

ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT

HEARING
BEFORE THE
SUBCOMMITTEE ON
COURTS AND ADMINISTRATIVE PRACTICE
OF THE
COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE
ONE HUNDRED FIRST CONGRESS

FIRST SESSION

ON

S. 46

**A BILL TO CLARIFY STANDARDS GOVERNING BANKRUPTCIES AND RE-
ORGANIZATIONS OF PUBLIC UTILITY COMPANIES UNDER TITLE 11 OF
THE UNITED STATES CODE**

JULY 26, 1989

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ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT

WEDNESDAY, JULY 26, 1989

**U.S. SENATE,
SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE,
COMMITTEE ON THE JUDICIARY,
*Washington, DC.***

The subcommittee met, pursuant to notice, at 10:07 a.m., in room SD-226, Dirksen Senate Office Building, Hon. Howell Heflin (chairman of the subcommittee) presiding.

Also present: Senators Thurmond and Grassley.

OPENING STATEMENT OF HON. HOWELL HEFLIN, A U.S. SENATOR FROM THE STATE OF ALABAMA

Senator HEFLIN. Good morning. Today the Subcommittee on Courts and Administrative Practice will hear testimony on S. 46, the Electric Utility Bankruptcy Clarification Act. This bill was introduced by Senator Rudman and Senator Humphrey on January 25, 1989. This legislation is in response to the bankruptcy of the Public Service of New Hampshire. PSNH is the largest electric utility in the State of New Hampshire. In 1972, the Public Service Co. of New Hampshire decided to build a nuclear powerplant at Seabrook.

Construction actually began in 1976. Since that time there have been numerous delays in construction for various reasons and the cost of construction has continued to rise. PSNH has invested over a billion dollars in the Seabrook project and because of severe cash flow shortages, the company filed bankruptcy in January 1988. In December 1988, PSNH filed a plan of reorganization which proposes to restructure the company in such a way as to bring the company partly under the control of the Federal Energy Regulatory Commission [FERC]. This is an attempt in part to allow the company to recoup some of its investment before Seabrook becomes operational.

We will hear testimony from individuals involved in both sides of the bankruptcy. It is the belief of the proponents of this legislation that S. 46 is necessary to ensure the State a permanent role in the reorganization of a public utility in order to protect the ratepayers and to maintain jurisdiction over public utilities.

Those opposed to S. 46 believe that S. 46 gives the State regulatory agency virtual veto power over a reorganization plan. While this legislation is immediately important to the State of New Hampshire, there is a larger issue to be addressed. What is the

State's role in Federal bankruptcy cases, and who should have the ultimate authority in confirming a plan of reorganization?

As noted earlier, PSNH has filed for chapter 11, and on June 30, the parties argued this issue before the bankruptcy judge. It is not our intent to influence the decision of the judge. That is why the subcommittee hearings were scheduled after the issue had been argued before the bankruptcy judge. It is my understanding that the judge's decision is expected sometime in mid-August. We have been asked to consider this legislation and in order to fully understand the merits of this legislation, it is necessary to hear from those who would be most directly affected by its passage.

I would like to welcome our witnesses to today's hearing, and especially my colleagues from the State of New Hampshire.

[A copy of S. 46 follows:]

101ST CONGRESS
1ST SESSION

S. 46

To clarify standards governing bankruptcies and reorganizations of public utility companies under title 11 of the United States Code.

IN THE SENATE OF THE UNITED STATES

JANUARY 25 (legislative day, JANUARY 3), 1989

Mr. HUMPHREY (for himself and Mr. RUDMAN) introduced the following bill;
which was read twice and referred to the Committee on the Judiciary

A BILL

To clarify standards governing bankruptcies and reorganizations of public utility companies under title 11 of the United States Code.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 That this Act may be cited as the "Electric Utility Bank-
4 ruptcy Clarification Act".

5 SEC. 2. (a) Chapter 1 of title 11, United States Code, is
6 amended by adding at the end thereof the following new
7 section:

8 "§ 110. Electric utility debtors

9 "(a) In cases in which the debtor is an electric utility,
10 the prior approval of any State regulatory authority vested

1 with jurisdiction over the electric utility operations, transac-
2 tions, properties or rates of the debtor shall be obtained
3 before the court may confirm any plan of adjustment or reor-
4 ganization or take any other action pertaining to the debtor
5 which would terminate or restrict the existing jurisdiction of
6 such State regulatory authority.

7 “(b) The pendency of any proceeding under this title
8 shall not be construed to nullify the jurisdiction or authority
9 of any State regulatory authority which would otherwise
10 apply to the operations, transactions, properties, or rates of a
11 debtor which is an electric utility.

12 “(c) For purposes of this section, the term ‘electric utili-
13 ty’ means any entity which owns or operates facilities used
14 for the generation, transmission, or distribution of electric
15 energy for sale, other than sale to tenants or employees of
16 the entity operating such facilities for their own use and not
17 for resale.”.

18 (b) The table of sections for chapter 1 of title 11, United
19 States Code, is amended by adding at the end thereof the
20 following:

“110. Electric utility debtors.”.

21 (c) This Act and the amendments made by this Act shall
22 become effective on the date of enactment and shall apply to
23 any case pending on such date.

Senator HEFLIN. Senator Grassley, do you have an opening statement?

**OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S.
SENATOR FROM THE STATE OF IOWA**

Senator GRASSLEY. I have an opening statement that I am going to put in the record, but I think that I want to emphasize something that is going to be weighty with me in this decision, and that is the fact that Congress is often implored by private litigants to preemptively give them a victory in the legislature. And in the case of bankruptcy laws, it is my understanding, Mr. Chairman, and I will rely upon you for having fuller knowledge of this, but that we have always turned down these requests in bankruptcy law and for good reason. And that does not mean that somewhere along the line you do not set a new precedent.

But it seems to me that there ought to be an overwhelming reason for doing that. So that is the way I am looking at this and approaching this issue, Mr. Chairman.

[The prepared statement of Senator Grassley follows:]

STATEMENT OF SENATOR CHARLES E. GRASSLEY
SUBCOMMITTEE ON COURTS
HEARING ON S. 46
REGARDING ELECTRIC UTILITY BANKRUPTCIES
JULY 26, 1989

MR. CHAIRMAN, THANK YOU FOR HOLDING THIS HEARING ON S. 46, THE ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT.

THE PROPONENTS OF THIS BILL BELIEVE THAT CURRENT LAW PERMITS A PUBLIC UTILITY DEBTOR TO PASS THROUGH TO THEIR CUSTOMERS UNJUSTIFIED RATE INCREASES AFTER THE UTILITY FILES FOR BANKRUPTCY PROTECTION.

TODAY, WE WILL HEAR NUMEROUS ARGUMENTS WHY CONGRESS SHOULD "CLARIFY" THAT STATE REGULATORY LAWS HAVING TO DO WITH ISSUES OTHER THAN RATES, SHOULD APPLY TO REORGANIZING ELECTRIC UTILITY DEBTORS. THE LAW ALREADY MAKES CLEAR THAT UTILITY RATES CHARGED BY A CHAPTER 11 DEBTOR MUST BE APPROVED BY STATE REGULATORS.

HOWEVER, THE REAL QUARREL FOR PROPONENTS OF THIS BILL IS WITH CHAPTER 11 ITSELF. CHAPTER 11 IS THE PRODUCT OF THE 1978 AMENDMENTS TO THE CODE. THE PLAIN GOAL OF CHAPTER 11 WAS TO STRIKE A BALANCE BETWEEN THE POWER OF DEBTORS AND THE RIGHTS OF CREDITORS. THIS BALANCE ENCOURAGES BOTH SIDES TO NEGOTIATE, A PROCESS FAVORED IN THE LAW, AND ONE THAT PROMOTES A MORE LASTING REORGANIZATION.

THE BEAUTY OF THIS BALANCE IS THAT EACH SIDE -- DEBTOR AND CREDITOR -- IS AT RISK. CREDITORS KNOW THAT A DEBTOR IN CHAPTER 11 CAN MODIFY CLAIMS AND OBLIGATIONS WHILE STILL REMAINING IN BUSINESS. DEBTORS KNOW THAT CREDITORS WILL HAVE A SUBSTANTIAL SAY IN HOW THE REORGANIZED BUSINESS WILL BE RUN. CREDITORS CAN ALSO SEEK TO BLOCK A PROPOSED PLAN. THE BALANCE STRUCK GIVES EACH SIDE REASON TO NEGOTIATE EARNESTLY, AND IN GOOD FAITH.

NEGOTIATIONS ARE WELL UNDERWAY IN THE NEW HAMPSHIRE CASE THAT IS THE GENESIS OF THIS BILL. THEY ARE ON-GOING IN THE CONTEXT OF THE BANKRUPTCY PROCEEDINGS BEFORE JUDGE YACOS. BUT THESE NEGOTIATIONS WILL BE MADE MOOT IF S. 46 BECOMES LAW. THEY ARE MADE MOOT BECAUSE S. 46 CLEARLY FAVORS ONE PARTY -- THE STATE OF NEW HAMPSHIRE -- TO THE PROCEEDINGS. INDEED, THE ENTIRE REORGANIZATION OF P.S.N.H. -- AS THE PEOPLE OF NEW HAMPSHIRE KNOW IT -- MAY BE MADE MOOT IF S. 46 BECOMES LAW.

CONGRESS IS OFTEN IMploRED BY PRIVATE LITIGANTS TO PRE-EMPTIVELY GIVE THEM A VICTORY IN THE LEGISLATURE. IN THE CASE OF BANKRUPTCY LAW, WE HAVE ALWAYS TURNED DOWN THESE REQUESTS, AND FOR GOOD REASON.

MR. CHAIRMAN, I HAVE AN OPEN MIND ABOUT THIS BILL. BUT IT IS THIS FEATURE OF S. 46 THAT GIVES ME THE MOST TROUBLE, AND I LOOK FORWARD TO HEARING THE JUSTIFICATION FOR THIS EXTRAORDINARY RELIEF.

Senator HEFLIN. Senator Thurmond, do you have an opening statement?

**OPENING STATEMENT OF HON. STROM THURMOND, A U.S.
SENATOR FROM THE STATE OF SOUTH CAROLINA**

Senator THURMOND. Yes, thank you, Mr. Chairman. Mr. Chairman, we are here today to consider S. 46, a bill introduced by Senator Humphrey and Senator Rudman. S. 46 would amend the Bankruptcy Code to allow for significant participation by a State regulatory authority when a public utility company seeks confirmation of a chapter 11 reorganization plan.

Specifically, S. 46 would require, in cases where the debtor in a chapter 11 reorganization is an electric utility, the prior approval of a State regulatory authority before the bankruptcy court may approve a plan of reorganization or take any action which could restrict a State's ability to regulate utility rates. S. 46 would become effective on the date of enactment and would apply to any cases pending on this date.

Under current law, though a State regulatory authority may participate to a limited degree in a chapter 11 proceeding, most aspects of the final reorganization plan for a bankrupt company may be confirmed without the prior approval of the State regulatory authority. S. 46, if enacted, would broaden the participation of State regulatory authorities in chapter 11 proceedings by requiring their prior approval before the bankruptcy court can confirm a plan of reorganization filed by an electric utility company.

As we consider amending the Bankruptcy Code, it must be done so only after comprehensive study because any modification may substantially affect the rights and liabilities of all parties to a bankruptcy proceeding. Therefore, S. 46 should receive this subcommittee's careful consideration. I look forward to hearing from all of our distinguished panelists as to the possible ramifications of this legislation. I hold these able Senators from New Hampshire in high esteem. We are very pleased to have them before our committee.

Senator HEFLIN. Well, we are delighted to have the two distinguished Senators from New Hampshire. Senator Rudman, I believe you are the author of the bill so if you will start.

Senator RUDMAN. Mr. Chairman, I am going to yield to Senator Humphrey. We both have meetings, but his is going on right now. So I am going to yield to him, and then I will follow him.

**STATEMENT OF HON. GORDON HUMPHREY, A U.S. SENATOR
FROM THE STATE OF NEW HAMPSHIRE**

Senator HUMPHREY. Thank you, Mr. Chairman, for the hearing and the opportunity to testify. As you pointed out, Senator Rudman and I were motivated to introduce this legislation by the situation in New Hampshire. The purpose of the legislation is simple: to preserve the efficacy of State laws protecting ratepayers against unwarranted utility rate increases.

The bottom line from our point of view is that a utility should not be able to evade those laws because it has placed itself in voluntary reorganization proceedings. Since we introduced S. 46, state-

ments supporting the legislation have been received from a wide variety of State utility commissions, Governors and consumers' groups, demonstrating that our bill addresses legitimate concerns extending well beyond the New Hampshire situation. Copies of those letters are attached to the testimony.

For example, Gov. John McKernan of Maine wrote to Chairman Biden as follows, regarding H.R. 681, the counterpart bill of S. 46, quoting:

As a result of Maine's recent exposure to two utility bankruptcies with the potential for serious disruption of the affordable supply of electricity, I am writing to urge your support of H.R. 681.

Similar letters have been received from the utility or public service commissions of the States of Indiana, New Jersey, Wisconsin, Arkansas, and New Hampshire. The letter from the Public Service Commission of Wisconsin expresses the sentiment reflected in these letters, stating as follows:

The Public Service Commission of Wisconsin is in full support of S. 46 and requests that it be supported. Wisconsin ratepayers could be seriously harmed should a Wisconsin electric utility adopt a course of action taken by the Public Service Co. of New Hampshire. It is important that Wisconsin ratepayers remain protected by our State reorganization statute.

And in a letter to Senators dated July 17, the consumer group, Public Citizen, stated:

S. 46 should not be seen as a New Hampshire bill. While the most immediate effect of the bill would be on ratepayers in New Hampshire, it would benefit ratepayers in almost every state in the union.

So, S. 46 is not a New Hampshire particular bill. Instead, the bill makes a modest and sensible adjustment to the Bankruptcy Code, which is supported by a wide variety of knowledgeable sources in the affected area of utility regulation.

PSNH reorganization provides a perfect illustration of why this bill is necessary. Under New Hampshire law, a utility cannot include the cost of construction works in progress in its rate base until the facility is generating electricity. PSNH has invested more than \$2 billion in the Seabrook facility, which is still not generating electric power. But PSNH's reorganization plan would have shifted regulation from the State Public Utility Commission to FERC, thereby preempting and nullifying New Hampshire's anti-CWIP law.

The purpose and the result of such a maneuver is obvious: to shift the cost of PSNH's soured investment in Seabrook to New Hampshire ratepayers, thus allowing the shareholders and unsecured bondholders to escape the downside risk of their investment and PSNH's bankruptcy.

The utility's lawyers will complain that our bill is unfair to PSNH and their investors. They will claim that the bill represents an unwarranted tinkering with the Bankruptcy Code. Mr. Chairman, to buy that argument, you have to agree that Congress intended the Bankruptcy Code to be used to sidestep State regulation because that is precisely what PSNH is trying to do. Congress never intended such a result. Companies which invoke special protections under the Federal Bankruptcy Code cannot claim that in

so doing they placed themselves beyond the reach of State regulatory agencies.

Finally, to claim that the bill constitutes a sharp departure from existing bankruptcy procedures simply does not hold water. For one thing, as has been pointed out in a study by the Congressional Research Service quoting:

There is no modern precedent for the reorganization of an investor-owned utility under the U.S. Bankruptcy Code.

Such reorganizations are unique. In other words, the existing Bankruptcy Code was not designed with a public utility company reorganization and bankruptcy in mind.

And for this reason, the CRS study concluded:

That the unique legal status of a highly regulated investor-owned utility and the critical product it provides may suggest that special legislative provision should govern its reorganization under the Bankruptcy Code.

Our bill is designed to address the very kind of gaps in the Bankruptcy Code which the CRS study identified. Moreover, the existing provisions of the Bankruptcy Code already require that State regulatory commissions with jurisdiction over the debtor must approve any rate change proposed in a reorganization plan before that plan can be confirmed.

S. 46 merely makes it clear that the reorganization plan cannot be structured to circumvent the authority of the State commission which had jurisdiction over the utility when it filed for reorganization.

These same considerations refute the argument that the bill should be rejected because its application to pending cases would be unfair or improper. For one thing, the application of newly enacted statutes to pending cases is the general rule, not the exception. As stated by the Supreme Court in the 1974 case, *Bradley versus School Board of Richmond*:

Even where the intervening law does not explicitly recite that it is to be applied to pending cases, it is to be given recognition and effect.

Of course, Congress may specifically provide that a statute should not apply to pending cases, but the justification for such provisions arises only where the new law would undercut existing precedents on which the parties have justifiably relied. But here there is no justified reliance on some settled practice or precedent. There is no established practice of precedent establishing that public utilities can avoid State regulations in bankruptcy by reorganizing as federally regulated entities.

This situation, Mr. Chairman, is novel and unique. And so it is entirely appropriate for Congress to fill in the gaps in the Bankruptcy Code which were not previously contemplated. In sum, S. 46 constitutes a modest and sensible modification of the Bankruptcy Code which is necessary for the protection of electric utility ratepayers, not only in New Hampshire but across the country. And therefore, I urge the committee to give prompt and favorable consideration to the bill. Thank you, Mr. Chairman.

[The statement of Senator Humphrey and additional material for the record follow:]

SENATE JUDICIARY COMMITTEE
SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE

HEARING ON S.46
ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT

STATEMENT OF SENATOR GORDON J. HUMPHREY

THANK YOU FOR ALLOWING ME TO MAKE A FEW INTRODUCTORY REMARKS ABOUT S. 46, THE ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT. I WOULD LIKE TO EXPRESS MY APPRECIATION TO SENATOR HEFLIN AND THE OTHER MEMBERS OF THE SUBCOMMITTEE FOR SCHEDULING TIMELY HEARINGS ON THIS IMPORTANT BILL.

IT IS NO SECRET THAT SENATOR RUDMAN AND I WERE MOTIVATED TO INTRODUCE THIS LEGISLATION BY THE SITUATION IN NEW HAMPSHIRE, WHERE PUBLIC SERVICE CO. OF NEW HAMPSHIRE IS PRESENTLY IN THE MIDST OF CHAPTER 11 REORGANIZATION PROCEEDINGS. OUR CONCERN IS THAT PSNH, AND OTHER UTILITY COMPANIES FACED WITH SIMILAR SITUATIONS, WILL USE THE REORGANIZATION PROCEDURES OF THE BANKRUPTCY CODE TO CIRCUMVENT STATE UTILITY REGULATIONS ENACTED TO PROTECT CONSUMERS. THE PURPOSE OF THIS LEGISLATION IS SIMPLE: TO PRESERVE THE EFFICACY OF STATE LAWS PROTECTING RATEPAYERS AGAINST UNWARRANTED UTILITY RATE INCREASES. A UTILITY COMPANY SHOULD NOT BE ABLE TO EVADE THOSE LAWS SIMPLY BECAUSE IT HAS PLACED ITSELF IN VOLUNTARY REORGANIZATION PROCEEDINGS.

SINCE WE INTRODUCED S.46, STATEMENTS SUPPORTING THE LEGISLATION HAVE BEEN RECEIVED FROM A WIDE VARIETY OF STATE UTILITY COMMISSIONS, GOVERNORS, AND CONSUMER GROUPS -- DEMONSTRATING THAT OUR BILL ADDRESSES LEGITIMATE CONCERNS EXTENDING WELL BEYOND THE PSNH SITUATION. (COPIES OF THESE LETTERS ARE ATTACHED TO MY PREPARED STATEMENT, WHICH I ASK BE INCLUDED IN THE RECORD) FOR EXAMPLE, MAINE GOVERNOR JOHN MCKERNAN WROTE TO CHAIRMAN BIDEN AS FOLLOWS CONCERNING H.R. 681, THE IDENTICAL HOUSE VERSION OF S.46:

"AS A RESULT OF MAINE'S RECENT EXPOSURE TO TWO UTILITY BANKRUPTCIES WITH THE POTENTIAL FOR SERIOUS DISRUPTION OF THE AFFORDABLE SUPPLY OF ELECTRICITY TO OUR STATE, I AM WRITING TO URGE YOUR SUPPORT OF H.R. 681, THE ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT....I FAVOR ENACTMENT OF H.R.681 DUE TO MAINE'S INTEREST IN EFFECTIVE STATE REGULATION OF ELECTRIC UTILITIES, PARTICULARLY IN CASES WHERE THOSE UTILITIES FACE AN UNCERTAIN AND TROUBLED FINANCIAL FUTURE."

SIMILAR LETTERS HAVE BEEN RECEIVED FROM THE UTILITY OR PUBLIC SERVICE COMMISSIONS OF THE STATES OF INDIANA, NEW JERSEY, WISCONSIN, ARKANSAS, AND NEW HAMPSHIRE. THE LETTER FROM THE PUBLIC SERVICE COMMISSION OF WISCONSIN EXPRESSES THE SENTIMENT REFLECTED IN THESE LETTERS IN STATING AS FOLLOWS:

"THE PUBLIC SERVICE COMMISSION OF WISCONSIN IS IN FULL SUPPORT OF S.46, AND REQUESTS THAT IT BE SUPPORTED BY YOU AND THE JUDICIARY COMMITTEE. WISCONSIN RATEPAYERS COULD BE SERIOUSLY HARMED SHOULD A WISCONSIN ELECTRIC UTILITY ADOPT THE COURSE OF ACTION TAKEN BY THE PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE WITH REGARD TO THE SEABROOK NUCLEAR POWER PLANT. IT IS IMPORTANT THAT WISCONSIN RATEPAYERS REMAIN PROTECTED BY OUR STATE REORGANIZATION STATUTE."

AND IN A LETTER TO SENATORS DATED JULY 17, THE CONSUMER GROUP PUBLIC CITIZEN AND THE U.S. PUBLIC INTEREST RESEARCH GROUP STATED:

"S.46 SHOULD NOT BE SEEN AS A "NEW HAMPSHIRE" BILL. WHILE THE MOST IMMEDIATE EFFECT OF THIS BILL WOULD BE ON RATEPAYERS IN NEW HAMPSHIRE, IT WOULD BENEFIT RATEPAYERS IN ALMOST EVERY STATE IN THE UNION."

SO ANY NOTION THAT S.46 IS JUST PAROCHIAL LEGISLATION CAN BE LAID TO REST. INSTEAD, THE BILL MAKES A MODEST AND SENSIBLE ADJUSTMENT TO THE BANKRUPTCY CODE WHICH IS SUPPORTED

BY A WIDE VARIETY OF KNOWLEDGEABLE SOURCES IN THE AFFECTED AREA OF UTILITY REGULATION.

WHILE S. 46 WILL PROVIDE BENEFITS BEYOND THE NEW HAMPSHIRE SITUATION, THE PSNH REORGANIZATION PROVIDES A PERFECT ILLUSTRATION OF WHY THIS BILL IS NECESSARY. UNDER NEW HAMPSHIRE LAW, A UTILITY CANNOT INCLUDE THE COSTS OF CONSTRUCTION WORK-IN-PROGRESS (CWIP) IN ITS RATEBASE UNTIL THE FACILITY IS GENERATING ELECTRICITY. PSNH HAS INVESTED MORE THAN \$2 BILLION IN ITS SEABROOK NUCLEAR FACILITY, WHICH IS STILL NOT GENERATING ELECTRIC POWER FOR CONSUMERS. BUT PSNH'S REORGANIZATION PLAN WOULD HAVE SHIFTED REGULATION FROM THE STATE PUBLIC UTILITY COMMISSION TO THE FEDERAL ENERGY REGULATORY COMMISSION, THEREBY HOPING TO PREEMPT AND NULLIFY NEW HAMPSHIRE'S ANTI-CWIP LAW.

THE PURPOSE AND RESULT OF SUCH A MANEUVER IS OBVIOUS: TO SHIFT THE COSTS OF PSNH'S SOURED INVESTMENT IN SEABROOK TO NEW HAMPSHIRE RATEPAYERS, THUS ALLOWING PSNH SHAREHOLDERS AND UNSECURED BONDHOLDERS TO ESCAPE THE DOWN-SIDE RISK OF THEIR INVESTMENTS AND PSNH'S BANKRUPTCY.

PSNH'S LAWYERS WILL COMPLAIN THAT OUR BILL IS "UNFAIR" TO PSNH AND ITS INVESTORS. THEY WILL CLAIM THAT S.46 REPRESENTS AN UNWARRANTED TINKERING WITH THE BANKRUPTCY CODE. TO BUY THAT ARGUMENT, MR. CHAIRMAN, YOU HAVE TO AGREE

THAT CONGRESS INTENDED THE BANKRUPTCY CODE TO BE USED TO
SIDESTEP STATE REGULATION.

OF COURSE, CONGRESS NEVER INTENDED SUCH A RESULT.
COMPANIES WHICH INVOKE THE SPECIAL PROTECTIONS OF THE FEDERAL
BANKRUPTCY CODE CANNOT CLAIM THAT IN SO DOING THEY PLACE
THEMSELVES BEYOND THE REACH OF STATE REGULATORY AGENCIES.
ONLY LAST YEAR, IN ENACTING THE MUNICIPAL BANKRUPTCY
AMENDMENTS, CONGRESS ADOPTED A NEW PROVISION REQUIRING THAT
ALL NECESSARY REGULATORY APPROVALS UNDER APPLICABLE
NONBANKRUPTCY LAW MUST BE OBTAINED BEFORE A PLAN OF MUNICIPAL
DEBT ADJUSTMENT CAN BE CONFIRMED BY THE BANKRUPTCY COURT.
S. 46 SIMPLY PROPOSES A SIMILAR REQUIREMENT FOR APPROPRIATE
STATE UTILITY AGENCY APPROVALS IN THE CASE OF AN ELECTRIC
UTILITY REORGANIZATION. THUS, OUR BILL SIMPLY BUILDS UPON
RECENT LEGISLATIVE PRECEDENT IN PROVIDING THAT LEGITIMATE
STATE UTILITY REGULATIONS CANNOT BE NULLIFIED SIMPLY BY
INVOKING THE PROCEDURES OF THE BANKRUPTCY CODE.

FINALLY, THE CLAIMS THAT THIS BILL CONSTITUTES A SHARP
AND DISRUPTIVE DEPARTURE FROM EXISTING BANKRUPTCY PROCEDURES
SIMPLY DON'T HOLD WATER. FOR ONE THING, AS HAS BEEN POINTED
OUT IN A STUDY BY THE CONGRESSIONAL RESEARCH SERVICE, "THERE
IS NO MODERN PRECEDENT FOR THE REORGANIZATION... OF AN
INVESTOR-OWNED UTILITY UNDER THE UNITED STATES BANKRUPTCY
CODE", AND SUCH REORGANIZATIONS ARE UNIQUE. IN OTHER WORDS,

THE EXISTING BANKRUPTCY CODE WAS NOT DESIGNED WITH PUBLIC UTILITY COMPANY REORGANIZATIONS AND BANKRUPTCIES IN MIND. FOR THIS REASON, THE CRS STUDY CONCLUDED THAT "THE UNIQUE LEGAL STATUS OF A HIGHLY REGULATED INVESTOR OWNED UTILITY, AND THE CRITICAL PRODUCT IT PROVIDES, MAY SUGGEST THAT SPECIAL LEGISLATIVE PROVISIONS SHOULD GOVERN ITS REORGANIZATION UNDER THE BANKRUPTCY CODE." S.46 IS DESIGNED TO ADDRESS THE VERY KIND OF GAPS IN THE BANKRUPTCY CODE WHICH THE CRS STUDY IDENTIFIED.

MOREOVER, THE EXISTING PROVISIONS OF THE BANKRUPTCY CODE (11 USC SEC 1129(a)(6)) ALREADY REQUIRE THAT STATE REGULATORY COMMISSIONS WITH JURISDICTION OVER THE DEBTOR MUST APPROVE ANY RATE CHANGE PROPOSED IN A REORGANIZATION PLAN BEFORE THE PLAN CAN BE CONFIRMED. S.46 MERELY MAKES IT CLEAR THAT THE REORGANIZATION PLAN CANNOT BE STRUCTURED TO CIRCUMVENT THE AUTHORITY OF THE STATE COMMISSION WHICH HAD JURISDICTION OVER THE UTILITY WHEN IT FILED FOR REORGANIZATION.

THESE SAME CONSIDERATIONS REFUTE THE ARGUMENT THAT S. 46 SHOULD BE REJECTED BECAUSE ITS APPLICATION TO PENDING CASES WOULD BE UNFAIR AND IMPROPER. FOR ONE THING, THE APPLICATION OF NEWLY ENACTED STATUTES TO PENDING CASES IS THE GENERAL RULE, NOT THE EXCEPTION. AS STATED BY THE SUPREME COURT IN THE 1974 CASE OF BRADLEY V. SCHOOL BOARD OF RICHMOND, "EVEN

WHERE THE INTERVENING LAW DOES NOT EXPLICITLY RECITE THAT IT IS TO BE APPLIED TO PENDING CASES, IT IS TO BE GIVEN RECOGNITION AND EFFECT." OF COURSE, CONGRESS MAY SPECIFICALLY PROVIDE THAT A STATUTE SHOULD NOT APPLY TO PENDING CASES, BUT THE JUSTIFICATION FOR SUCH PROVISIONS ARISES ONLY WHERE THE NEW LAW WOULD UNDERCUT EXISTING PRECEDENTS ON WHICH THE PARTIES HAVE JUSTIFIABLY RELIED. BUT HERE THERE IS NO SUCH JUSTIFIED RELIANCE ON SOME SETTLED PRACTICE OR PRECEDENT. THERE IS NO ESTABLISHED PRACTICE OR PRECEDENT ESTABLISHING THAT PUBLIC UTILITIES CAN AVOID STATE REGULATIONS IN BANKRUPTCY BY REORGANIZING AS FEDERALLY-REGULATED ENTITIES. THIS IS A NOVEL AND UNIQUE BANKRUPTCY SITUATION, SO IT IS ENTIRELY APPROPRIATE FOR CONGRESS TO FILL IN THE GAPS IN THE BANKRUPTCY CODE WHICH WERE NOT PREVIOUSLY CONTEMPLATED.

IN SUM, S.46 CONSTITUTES A MODEST AND SENSIBLE MODIFICATION OF THE BANKRUPTCY CODE WHICH IS NECESSARY FOR THE PROTECTION OF ELECTRIC UTILITY RATEPAYERS. I URGE THE COMMITTEE TO GIVE PROMPT AND FAVORABLE CONSIDERATION TO THIS LEGISLATION.



State of Wisconsin

PUBLIC SERVICE COMMISSION

CHARLES H. THOMPSON, CHAIRMAN
 MARY LOU MUNTZ, COMMISSIONER
 CHERYL L. POFAHL, COMMISSIONER
 4802 Sheboygan Avenue
 P. O. Box 7854
 Madison, Wisconsin 53707

April 13, 1989

Honorable Joseph R. Biden, Jr.
 Chairman, Committee on Judiciary
 United States Senate
 489 Russell Senate Office Building
 Washington, D. C. 20510

RE: S. 46 -- A bill proposing to prevent electric utilities from
 declaring bankruptcy to circumvent state law.

Dear Chairman Biden:

The Public Service Commission of Wisconsin is in full support of S. 46, and requests that it be supported by you and the Judiciary Committee. Wisconsin ratepayers could be seriously harmed should a Wisconsin electric utility adopt the course of action taken by the Public Service Company of New Hampshire with regard to the Seabrook Nuclear Power Plant. It is important that Wisconsin ratepayers remain protected by our state reorganization statute. Therefore, we request that you support Senator Humphrey's clarifying legislation.

Thank you for your consideration.

Sincerely,

Charles H. Thompson

Charles H. Thompson
 Chairman

Mary Lou Muntz

Mary Lou Muntz
 Commissioner

Cheryl L. Pofahl

Cheryl L. Pofahl
 Commissioner

cc: Judiciary Committee Members
 Senator Herbert Kohl
 Senator Robert Kasten
 Paul Rodgers, NARUC
 Julianne Wood, NARUC

JFE:vml:S46COMM.LTR



STATE OF NEW JERSEY
BOARD OF PUBLIC UTILITIES

CHRISTINE T. WHITMAN
PRESIDENT

TWO GATEWAY CENTER
NEWARK, N.J. 07102
201-648-2027

April 12, 1989

Honorable Gorden J. Humphrey
United States Senator
Washington, DC 20510

RE: S.46 and HR. 681, Bills Proposing to Prevent Electric
Utilities from Declaring Bankruptcy to Circumvent State Law

Dear Senator Humphrey:

The New Jersey Board of Public Utilities is concerned about the precedent being set by Public Service Company of New Hampshire's (PSNH) filing for Bankruptcy and Reorganization under Chapter 11 of the United States Code. It has come to our attention, through the National Association of Regulatory Utility Commissioners, that PSNH is seeking reorganization in order to circumvent state regulation.

This Board supports the passage of S. 46 and H.R. 681 which are designed to prevent such action by utilities. It is our belief that clarification of the bankruptcy law to require prior state regulatory approval for plans of adjustment or reorganization is a positive action.

Thank you for considering our comments on this important issue.

Very truly yours,

Christine Todd Whitman,
President

SI/peb/Elec.

CTW No. 208-89

C: Julianne Wood
Paul Rogers



STATE OF MAINE
OFFICE OF THE GOVERNOR
AUGUSTA, MAINE
04801

JOHN R. MCKERNAN, JR.
GOVERNOR

April 12, 1989

Honorable Joseph R. Biden, Jr.
SD-224
Washington, D.C. 20510-2675

Dear Senator Biden:

As a result of Maine's recent exposure to two utility bankruptcies with the potential for serious disruption of the affordable supply of electricity to our state, I am writing to urge your support of H.R. 681, the Electric Utility Bankruptcy Clarification Act. This bill provides that bankruptcies and reorganizations of public utilities will not short-circuit state regulatory jurisdiction. In the course of a recent reorganization filing under Chapter 11 of the Bankruptcy Code made by Public Service of New Hampshire, that utility has proposed that federal regulatory oversight of a newly-created holding company should supersede state jurisdiction over costs associated with the Seabrook nuclear power plant. A Maine consumer-owned electric utility, the Eastern Maine Electric Cooperative, has filed for protection under Chapter 11 as well, due to its inability to support continued investment in the Seabrook project.

I favor enactment of H.R. 681 due to Maine's interest in effective state regulation of electric utilities, particularly in cases where those utilities face an uncertain and troubled financial future. The federal government and courts have for years recognized the importance of state regulation of electric utility operations. In the absence of H.R. 681's enactment, this important state interest could be jeopardized in pending - and future - bankruptcy proceedings.

Thank you for your attention to this very important concern.

Sincerely,

John R. McKernan, Jr.
Governor

JRM/mpm

cc: Maine Congressional Delegation

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION
815 STATE OFFICE BUILDING

INDIANAPOLIS 46204-2264

April 10, 1989

The Honorable Richard G. Lugar
306 Hart Building
Washington, D.C. 20510

RE: S. 46 Senator Gordon Humphrey

Dear Senator Lugar:

The Indiana Utility Regulatory Commission would like to express our strong support for S. 46 introduced by Senator Gordon Humphrey entitled the "Electric Utility Bankruptcy Clarification Act". Senator Humphrey's bill addresses a problem in New Hampshire where Public Service Company of New Hampshire has sought protection of the bankruptcy court. The PSNH bankruptcy is the result of problems emanating from the long delay in issuing an operating license to the Seabrook Nuclear Power Plant.

In March of 1986, this Commission by emergency action following lengthy proceedings granted Public Service Indiana emergency rates which, in conjunction with numerous other provisions of the Order, saved PSI from bankruptcy. One of the reasons that this Commission determined it to be essential that PSI not become bankrupt is the very problem addressed by Senator Humphrey's bill. That question is the extent to which a bankruptcy court might go in setting rates for a utility's electric customers contrary to the orders of the state's legitimate ratemaking agency, in our case the Indiana Utility Regulatory Commission.

Although PSI avoided bankruptcy as a result of the closing down of the Marble Hill construction, the Wabash Valley Power Association which held a 17% interest in that new construction, was forced into bankruptcy more specifically a Chapter 11 proceeding. The major problem now facing WVPA in those proceedings are the claims of the Rural Electrification Administration that it has the power to override state jurisdictions and to order WVPA in spite of the IURC and without express authority from anyone, including the bankruptcy court, to raise its electric rates to a level deemed sufficient by the REA.

This very brief and oversimplified review of our situation in Indiana should help you to understand why the IURC considers S. 46 or similar legislation to be very important. As a matter of fact, while S. 46 may meet the New Hampshire crisis it really is not broad enough to address the current conflict between the IURC and REA. Regardless of that concern, however, we strongly support the remedy provided by S. 46 in that it would definitely clarify the position of all parties insofar as bankruptcy proceedings of a

public utility are concerned.

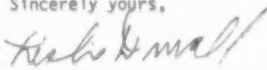
Presently WVPA has pending before the United States District Court for the Southern District of Indiana in civil action IP 89-126-C its complaint for declaratory judgment against the Rural Electrification Administration to settle this jurisdictional question. I am enclosing for you and your staff a copy of this complaint in order that you may better understand WVPA's position in this matter, a position with which the IURC is fully in accord. Frankly, we consider the manner in which the Rural Electrification Administration is addressing this problem to be an example of federal bureaucracy at its worst. You are probably already aware of the fact that REA has advised WVPA's member cooperatives that no further financial assistance will be extended until the member cooperatives comply with REA's orders. The IURC is seeking to intervene in these federal court proceedings in support of WVPA.

While we are very optimistic that WVPA will prevail in the declaratory judgment action, it seems preferable that such confrontations be resolved either by changes in policy or, if that is not possible, federal legislation.

A number of Indiana utilities are subsidiaries of holding companies. Although none seems in current danger of bankruptcy, the situation addressed by S. 46 could occur in Indiana at some future date. We urge your support of S. 46 and any amendments which might further strengthen the bill.

The Commission and its Staff will be very happy to provide you with any additional information which you might wish in regard to this problem.

Sincerely yours,



Leslie Duvall
Acting Chairman

gk

Enclosure

c: Commissioners Corban, Bailey, Zagrovich, O'Lessker
Senator Gordon Humphrey
Honorable Vincent Iacopino
Paul Rodgers, National Association of Regulatory Utility
Commissioners

STATE OF NEW HAMPSHIRE



CHAIRMAN
Vincent J. Iacopino

COMMISSIONERS
Bruce B. Ellsworth
Linda G. Blason

PUBLIC UTILITIES COMMISSION

8 Old Suncook Road
Concord, N.H. 03301-5105

EXECUTIVE DIRECTOR
AND SECRETARY
Wynn E. Arnold
Tel. (603) 271-2431

July 21, 1989

Honorable Gordon J. Humphrey
U.S. Senator
Washington, D.C. 20510

Dear Senator Humphrey:

The New Hampshire Public Utilities Commission would like to express our support for S.46 which you have introduced for action by the Congress.

We feel that your proposed legislation is essential for the protection of the ratepayers of the State of New Hampshire and for the recognition by the federal government of the States' right to handle such matters. This Bill would clarify the fact that bankruptcy courts would not, and could not, supercede or pre-empt state control of public utilities operating under their jurisdiction. The commission feels that utility companies may use the Bankruptcy Court to try and circumvent state control and obtain more advantageous treatment at the federal level.

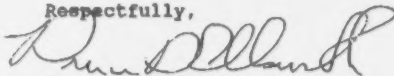
Recently Public Service Company of New Hampshire (PSNH) filed for bankruptcy and re-organization under Chapter 11 of the United States Code. During the course of the proceedings, the Bankruptcy Court has made certain rulings pre-empting our control over PSNH. Specifically the Court has not provided for the return of security deposits held for commercial customers although this commission ordered such a return, and the State, though the Attorney General's Office has petitioned for the return of said deposits for over a year. The Court has enjoined a rate examination of PSNH when it became apparent to the commission that the company was exceeding its approved rate of return. And most importantly, the Court is considering allowing PSNH to form a public utility holding company subject only to federal regulation, where state law specifically requires our approval for such re-organizations.

The commission has serious concerns regarding the re-organization plan, as PSNH serves over seventy-five percent of the electric customers in the State of New Hampshire. We feel it

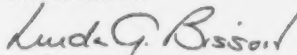
- 2 -

is necessary that the Bankruptcy Code be clarified so that state regulatory commissions retain jurisdiction over utility companies serving the residence of their state as said state commissions are closer to the people being served and the companies providing service.

Respectfully,



Bruce B. Ellsworth
Commissioner



Linda G. Bison
Commissioner

/dec



Jerrell L. Clark
Director
682 1794

ARKANSAS
PUBLIC SERVICE COMMISSION

1000 Center
P.O. Box C-400
LITTLE ROCK 72203

Robert E. Johnston
Chairman
682 1453

Patricia S. Qualls
Commissioner
682 1451

Julius D. Kearney
Commissioner
682 1455

April 27, 1989

The Honorable Dale Bumpers
U. S. Senator
SD-229 Dirksen Senate Office Bldg.
Washington, DC 20510-0401

Dear Senator Bumpers:

On January 25, 1989, Senator Gordon Humphrey introduced S. 46. This legislation would prevent electric utilities from using the reorganization provisions of the bankruptcy code to circumvent State laws governing rates and other matters.

The Arkansas Public Service Commission supports this legislation. However, we are concerned that the definition of electric utility used in §110.(c) hits more than was intended. It appears that a broad interpretation of this section could potentially include co-generation facilities. Under the Public Utility Regulatory Policy Act, the utility that ordinarily supplies a co-generation facility with electricity is required to buy any excess electricity produced by a co-generation facility. This could possibly bring these co-generation facilities in under the resale provision.

The Arkansas Public Service Commission urges you to support S. 46 with an amendment specifically exempting the co-generation facilities.

Thank you for your consideration in this matter.

Sincerely,

Sam I. Bratton, Jr.
Sam I. Bratton, Jr., Chairman

Pat Qualls
Patricia S. Qualls, Commissioner

Julius D. Kearney
Julius D. Kearney, Commissioner

cc: The Honorable Gordon Humphrey

Senator HEFLIN. Would you like us to direct any questions we have for Senator Humphrey at this time so he can leave?

Senator RUDMAN. Why do you not ask Senator Humphrey what you would like, and then I can proceed.

Senator HUMPHREY. Do any of you have any questions of Senator Rudman?

Senator THURMOND. Yes, I have a few questions.

Senator HEFLIN. Go ahead, Senator Thurmond.

Senator THURMOND. I might just ask this question, and each one of you can express your opinion. Some have asserted that by setting up a holding company which is subject to the jurisdiction of the Federal Energy Regulatory Commission, the Public Service Co. of New Hampshire is attempting to use reorganization to circumvent the State of New Hampshire regulatory system.

Do you believe this is the case, and if so, is amending the Bankruptcy Code the only way to protect consumers from potential sharp increases in utility rates?

Senator HUMPHREY. That is precisely the situation, precisely the difficulty that we are seeking to remedy. Public Service Co. of New Hampshire, I think it is fair to say, made an investment which at least in retrospect turned out to be a very bad investment and resulted in the bankruptcy of that utility. Now the utility is seeking to reorganize so that it will be regulated by FERC and may pass through to the ratepayers without State authorization whatever rate increases are necessary to protect the shareholders and the unsecured bondholders. In other words, they are seeking to shift the burden to the ratepayers who have had no say in this investment and off the shoulders of the shareholders and the others who should rightly bear the burden in a bankruptcy proceeding.

Senator THURMOND. Senator, would you care to answer?

Senator RUDMAN. Senator Thurmond, I will address that in my statement in great detail. So I am going to hold until then.

Senator THURMOND. It has been projected that the Seabrook Nuclear Power Plant may be operational in the spring of 1990. Once the Public Service Co. of New Hampshire's reorganization plan has been confirmed and Seabrook is operational, what protections will ratepayers have in the State of New Hampshire as a result of enacting S. 46?

Senator HUMPHREY. The utility will continue to come under the regulation of the State Public Utility Commission which will take all arguments into consideration in the setting of rates. If this bill does not pass, the utility probably will succeed in reorganizing such that its rates will be set by the FERC, Federal Energy Regulatory Commission.

Senator THURMOND. I had a couple questions more I was going to ask you, but I can wait until Senator Rudman introduces his testimony. Thank you very much.

Senator HUMPHREY. Thank you, Mr. Chairman.

Senator HEFLIN. Senator Grassley.

Senator GRASSLEY. Thank you for your testimony. I do not have any questions of you at this point.

Senator HUMPHREY. May I excuse myself? There is a meeting in Senator Dole's office which I am supposed to be attending, if you do not mind?

Senator HEFLIN. That is what we are trying to arrange.

Senator HUMPHREY. Thank you and my apologies to all.

Senator HEFLIN. All right. Senator Rudman, if you will proceed, we are delighted to hear from you now.

**STATEMENT OF HON. WARREN B. RUDMAN, A U.S. SENATOR
FROM THE STATE OF NEW HAMPSHIRE**

Senator RUDMAN. Mr. Chairman and Senator Grassley, Senator Thurmond, thank you very much for giving us the opportunity to appear this morning. I will apologize for the length of this statement, but I have attempted to put together a comprehensive statement because this is the initial hearing on this, and thus I will probably go on for 10 or 12 minutes, but I believe when I am finished, it should answer some of the questions that you may have.

Senator HEFLIN. Please try to summarize; we will place your entire statement in the record.

Senator RUDMAN. Mr. Chairman, on January 29, 1988, Public Service Co. of New Hampshire, the State's largest public electric utility, filed for bankruptcy, becoming the first major investor-owned utility to file bankruptcy since the Great Depression. Because of the enormous cost overruns incurred by PSNH in constructing the Seabrook plant combined with a State statute restricting construction-work-in-progress costs from being charged back to the taxpayers, this led to PSNH seeking protection under chapter 11.

On December 27, 1988, the company submitted a reorganizational plan which attempts to use the bankruptcy statute to justify the Federal preemption of State regulation of utility rates. It does this under the guise of reorganization by switching rate regulation from the New Hampshire PUC to FERC. As the Public Service Co. stated in their annual report, and I quote:

Rate increases would have to come from a shift in a portion of rate regulation of the company from the PUC to FERC.

Since FERC allows CWIP charges, that is utilities to charge for the costs of plants not yet in operation, Public Service Co. would be able to avoid the 11-year-old State statute prohibiting that from happening. Getting out from under State law is the only purpose, and I repeat, the only purpose of Public Service Co.'s efforts.

This preemption which Public Service Co. attempts to justify in its memorandums before the bankruptcy court is completely outrageous. If Public Service Co. and its creditors are allowed to preempt State regulation by manipulating the Bankruptcy Code to this end, I predict there will be a flood of utilities across this country filing for voluntary protection under chapter 11 in order to gain rate relief from State regulators and assure higher profits for its stock and bondholders.

Congress never intended to allow the Bankruptcy Code to completely disregard the public interest, in this case, captive electric consumers. The protection of creditors and investors is not the only interest to be considered in a bankruptcy proceeding and current law does recognize that.

Current Federal law clearly demonstrates the intent of Congress that applicable statutes and regulations should continue to apply to

companies in bankruptcy while conducting their business. For example, the public is protected from violations of environmental, health and safety laws, and regulations by bankrupt companies.

Regrettably, the Bankruptcy Code may not be sufficiently explicit to prevent a court from circumventing Congress' intent in the case of a regulated utility seeking to avoid State law relating to electric rates. This is not a great shock. Nobody conceived of bankrupt utilities during consideration of bankruptcy laws in recent years. As I noted, the last one occurred over 50 years ago.

Attorneys representing Public Service now assert by using in my view smoke and mirrors that a bankruptcy court has the authority to violate all of our federalist principles. In a briefing book analyzing S. 46, Public Service lawyers rely on the Bankruptcy Reform Act of 1978, and the Bankruptcy Amendment Act of 1984 to make the case that Congress:

* * * significantly reduced control of nonbankruptcy regulatory bodies because it found the process of regulatory approval too cumbersome and inflexible.

The Public Service Co. analysis goes on to argue that by enacting section 1123(a) relating to the content of a reorganizational plan, which begins, in part, "Notwithstanding any otherwise applicable non-bankruptcy law," Congress clearly intended for Federal bankruptcy law to preempt any otherwise applicable State law and regulation.

Their argument is so broad as to suggest the right of a bankruptcy judge to waive State environmental laws, health and zoning regulations, and it is wrong in this case. There is little doubt that Congress wanted to retain State and Federal authority over utility rates. Section 1129 of chapter 11 of the code requires the regulatory authority with jurisdiction over the rates of the debtor to approve a reorganization plan that includes rate increases.

And that is very important, and I hope that the subcommittee and staff will look at section 1129. If anything clearly points out that bankruptcy courts were not to take jurisdiction over the setting of rates, then this section shows as clearly as any. What we have here on the part of this company is a backdoor attempt through a reorganization to accomplish the same thing.

To put this whole thing into very plain English, the law says that if a rate change is part of a reorganization plan, the regulatory authority with jurisdiction over rates, in this case, the State of New Hampshire, must approve the rate change.

Public Service Co. knows that, but argues it is instead acceptable to use the bankruptcy statute to terminate a portion of the State rate-making authority by transferring it to FERC. Their argument defies common sense. S. 46 merely requires the approval of the State regulators over rates and other utility operations in a bankruptcy plan which terminates or restricts State authority before such a plan may be approved by a court.

It would clarify what I believe was the intent of Congress all along. Namely, that the State utility laws continue to apply in bankruptcy proceedings. The Public Service Co. analysis asserts that S. 46 is retroactive, and that the application of the bill to the company bankruptcy case is:

* * * at odds with a purposeful and long-standing congressional practice that has largely avoided changing the rules in ongoing bankruptcy proceedings.

Mr. Chairman, I disagree. S. 46 simply restates what everyone believed the law to be until a few lawyers started to muddy the waters. S. 46 simply clarifies the intent of the Congress as to the role of State regulatory authorities under existing law.

Mr. Chairman, as anyone who deals with utility regulation knows, there is what is known as a regulatory compact between the regulator and the regulated that in exchange for running a monopoly in a service area, an electric utility is guaranteed a fair and reasonable profit. Public Service Co. has argued throughout the bankruptcy proceeding that because investments in Public Service were made under this compact, creditors and investors should be paid in full.

I do not argue with the notion that if an investment in a utility was made with the expectation that it was a relatively safe investment with a reasonable return, then that investor should be given consideration by the bankruptcy court. However, it is preposterous to suggest that holders of speculative junk bonds currently demanding full payment in this bankruptcy case have a right under Federal law to be repaid in full. These speculators, and that is what they are, knew full well the uncertainty of their investment in Public Service Co. and the Seabrook facility. In fact, the prospectus for those bonds mostly issued 7 years or more after the adoption of New Hampshire's anti-CWIP law and when licensing of Seabrook was highly speculative, stated on their face these are speculative investments.

Clearly, these bonds were not bought with a regulatory compact in mind. They were made because of the high rates of interest being offered, in some cases 21 percent. I just repeat that for the committee, 21 percent on a utility bond. And their sale at discount prices in some cases those bonds sold, Mr. Chairman, for 30 cents on the dollar. I think we can take notice of the fact these are not your normal utility investments.

Now this company using the Bankruptcy Code as justification argues that these bondholders should be repaid by preempting State law in order to ensure a drastic increase in electric rates. Public Service seriously suggests that Congress intended for the bankruptcy process to be used to bludgeon captive electricity customers.

I strongly disagree. This company's reorganization plan is a brain child, and I hesitate to use such strong language, but I will, it is the brain child of greedy Wall Street bondholders who care not a whit about New Hampshire, its consumers, or its economic future. These investors hope that by manipulating the bankruptcy statutes, they can reap huge profits in their investment. I ask you, Mr. Chairman, and others members of this subcommittee, should the New Hampshire ratepayers be forced to pay and pay dearly to remove the risk from junk bonds purchased by speculators? Did Congress intend for the Bankruptcy Code to be abused in this way? I suspect your answer will be similar to my own, a strong and affirmative "no."

Consumers had no input in the management decisions of Public Service Co., particularly the decision to continue constructing the

Seabrook facility following enactment of the anti-CWIP law in 1978, 10 years before the company filed for protection under chapter 11. The company argues that because the State of New Hampshire encouraged the construction of Seabrook and the PUC approved continued financing of the plant, that consumers should now bear the brunt of its cost overruns.

In their lengthy briefing book, they omit the fact that the Public Utilities Commission of New Hampshire attempted in 1982 to gain control over the financial decisions relating to construction of that plan. The New Hampshire Supreme Court decided that Public Service Co. had the right to complete the plant without any input from that regulatory commission, essentially gagging the input of consumers over the construction of the Seabrook plant. I do not quarrel with that decision now. That was a decision of a court, but it did mean that the company on its own without any input from State regulators decided to take the risk and proceed with the plant and pay 21 percent on some of its investor bonds. The company, not the State or the consumers, made that decision to issue those securities, the holders of which now cry out the loudest in these proceedings for profits on their investments.

This reorganization plan would change the rules in favor of the bondholders by forcing consumers to bear the brunt of their risk. Congress should never condone the use of the bankruptcy court to place an undue burden on the only constituency that is not adequately represented in the bankruptcy process. A constituency that would under this plan shoulder the financial consequences of bad management decisions and risky investments over which they had little or no control. While S. 46 would prevent the transfer of regulatory authority to take place in New Hampshire through chapter 11 without the approval of the State PUC, it is not meant to be limited just to our State. If the bankruptcy court allows the preemption of State regulation over rate making, other utilities will follow this company in lock-step. Senator Humphrey has mentioned others who support this.

Mr. Chairman, let me conclude. We must protect electricity consumers from a process which is not considered their interest but rather favors those of the investor and the creditor. Congress intended for the public interest to be considered in the case of a bankrupt public electric utility. While the current Bankruptcy Code already contains provisions concerning electric rates, our legislation would further clarify these provisions to protect the public interest and close the loophole which Public Service Co. and its creditors believe they have found.

The bill, if enacted, would assure consumers who could otherwise be held hostage by the bankruptcy court without any input from the State agency with jurisdiction over rates that their interest will be considered prior to the confirmation of a plan. Finally, Mr. Chairman, in a memoranda before the bankruptcy court, Public Service Co. of New Hampshire characterized the introduction of S. 46 by the New Hampshire congressional delegation as "disingenuous" and a "charade." The only people that are being disingenuous are Public Service Co. and its creditors in their strained attempt to preempt proper State regulatory authority over rate making.

Their effort to rob the ratepayers of New Hampshire demonstrates the worst kind of greed and violation of public trust. I urge the subcommittee to put an end to this effort by favorably reporting to the floor S. 46 where I am sure it will receive a hospitable reception. I am happy to answer your questions.

Senator HEFLIN. Senator Rudman, as a former attorney general, I suppose you were involved in appeals from the State regulatory agency to the Supreme Court. I am trying to recall some of the principles involved, and I realize that they vary from State to State. But as I remember generally, when an appeal was sought by a utility, based on the fact that the rate base was too low, the issue was whether or not it was a constitutional taking of property, in that a fair and reasonable rate was not allowed. The Supreme Court would, in effect, establish a reasonable rate based on the expert testimony.

Now, is the appeal from a State supreme court either by the ratepayers, if they have a right, or the attorney general representing ratepayers, or the utility, to the Supreme Court of the United States a matter of certiorari? Is that correct?

Senator RUDMAN. Well, Mr. Chairman, my experience in New Hampshire, and I had a great deal of it with appeals to the Supreme Court from the Public Utilities Commission in cases of health insurers, telephone companies, electric utility companies, was that the State supreme court was the final arbiter and that is where it stopped. Of course, this case has been in and out of the Supreme Court in a variety of ways, the Supreme Court of New Hampshire, not only on the issue of rates, but the case which I cited in my testimony which was a fascinating case. The State Public Utilities Commission said we believe we have a right to tell you when you may be getting beyond good judgment in our view in terms of your investments. The Public Service Co. said no, you do not have that right.

We have a right to build this plant the way we want to build it. You have a right, Public Utilities Commission, when we are all done, to tell us what rate we can charge, and they won, and they went ahead and issued junk bonds and so forth. Now, of course, they are saying, no, we do not want the Public Utilities Commission to regulate us in New Hampshire. We want it done by FERC because, you see, in New Hampshire, the Public Utilities Commission cannot take the anti-CWIP statute into effect.

So you are quite right. New Hampshire is like Alabama, or other States where the State supreme court is the final stop along the way. I do not know of any cases in our State—there may be others—where it went to another court after our supreme court.

Senator HEFLIN. Well, I am trying to determine the Federal jurisdiction of any other courts. Other than by writ of certiorari to the Supreme Court, there is no way that either ratepayers or the attorney general in behalf of ratepayers or the utility can get jurisdiction in the U.S. district courts or in the circuit courts of appeal?

Senator RUDMAN. I think the chairman is correct. I do not believe we could. And further I would point out here that if this reorganization took place and you will hear this from the utility lawyers. Talk about disingenuous statements, they are going to say, oh, no, the Public Utilities Commission will continue to have juris-

diction over the retail rates, but the wholesale rate will be set by FERC.

Well, of course, if the wholesale rate comes into the State of New Hampshire at "x," then under our State law, the State regulatory bodies are forced to accept that no matter what level it is at and then pass it on to consumers with whatever other regulation they wish to apply. So this will be no appeal. If this ever gets to FERC, for all intents and purposes, bureaucrats down here in Washington will be setting the utility rate for consumers in Manchester, NH.

I dare say you would not want that to happen to Montgomery or in Columbia, and we do not want it to happen in Manchester. We want New Hampshire people with New Hampshire political process to have something to say about what New Hampshire people pay for electric rates, not bureaucrats sitting down here on 16th Street someplace.

Senator HEFLIN. Well, I just wanted to clarify the jurisdiction of the Federal courts. Really, from the viewpoint of the State, the bankruptcy court, in effect, is the only Federal court that would have jurisdiction.

Senator RUDMAN. That is correct, and under the present bankruptcy law, if this company went into bankruptcy, chapter 11, the State Utilities Commission still has control over rates, but of course, this is a backdoor approach. They are trying to get around that and take it on down here to FERC, and it is pretty clever, pretty inventive. The lawyer who thought of it certainly has earned his fee. I do not think he is going to succeed.

Senator HEFLIN. The utility is the only party, in effect, that can file bankruptcy from a practical viewpoint. Now let us assume a hypothetical case. I am trying to understand the principles involved here.

Assume a hypothetical case in which the regulatory agency denies a reasonable and fair return. The court affirms the decision, and as a result of that, after several years, the utility becomes insolvent and files bankruptcy. The utility then files a plan of reorganization. Under present law, the bankruptcy judge could confirm a plan of reorganization which, in effect, either directly or indirectly raised rates. Am I correct in that?

Senator RUDMAN. I think it would be indirectly. There are people in this room who are more expert than I on that subject. As I read section 1189, I think that the State Regulatory Commission still holds control. You get into kind of a political gridlock at that point, it seems to me.

Lawyers for the State of New Hampshire are here who have represented the State. They are going to be here. Our State attorney general is here, and they might be able to testify on that more accurately than I, but I would represent to you that under present law, even with the bankruptcy going on, the State of New Hampshire Public Utilities Commission, and the State supreme court have authority, and I do not know what the bankruptcy judge—I do not think the bankruptcy judge can by himself issue new electric rates. I do not believe that he can. Now somebody may want to disagree. I do not believe so.

Senator HEFLIN. Well, if the utility is insolvent—I would assume that the only way you could have a plan of reorganization that

would bring the debtor out of insolvency, would be if the plan proposed an increase of revenue to the utility.

Senator RUDMAN. I believe you are absolutely correct. I believe the chairman is correct, and no one in New Hampshire expects that will not happen. The question is whether or not it is going to include paying off people with the kind of investments I described. Thereby, instead of raising the rates by maybe 5, 6, 7 percent a year, having rate shock that would have sticker shock comparable to the B-2.

Senator HEFLIN. Now, there has been some criticism by the opponents of this bill because of the retroactive provision. The opponents argue that if Congress were to enact this bill, it would substantially alter the outcome of the pending bankruptcy. This issue of retroactivity has arisen on many occasions. What public policy concerns do you think Congress should consider before intervening in an ongoing case?

Senator RUDMAN. Mr. Chairman, I believe that my position on that has long been clear. In fact, I have had some interesting battles on the floor saying that I do not believe that retroactivity ought to apply. You ought not to take a case that is being interpreted under understandable current law and then try to change the law after the case is pending. But this is not that kind of a case.

And you know it is the great cry of the opponents of this legislation that, oh, you are trying to intervene in current proceeding. That is true. We are. But the reason we are, there were two reasons. No. 1, this bankruptcy law is being used inventively by people who know what they are doing in a way that no one in Congress ever intended. No one, if you go back and look at any of the bankruptcy code hearings, records, whatever, 1978, you will not find anything regarding this kind of maneuver.

What they are doing here is essentially saying to the bankruptcy judge we are not asking you to set the electric rates for the State of New Hampshire. We are just asking you to allow us to reorganize under Federal law, and once he approves that, which he has the authority to do, I suppose, subject to appeal of the courts, et cetera, then they have achieved their purpose.

So all we are trying to do is to clarify what we believe the bankruptcy code now indicates, namely, that the federalist principles apply in a bankruptcy proceeding, namely, that the State Regulatory Commission ought to continue to hold jurisdiction. That is what we are doing. We are not going retroactively at all.

We are trying to make sure there is a clarification where in our view there is an abuse in interpretation of this. Now it is only an abuse if the court issues it. We do not know what the court will do, but we believe Congress ought to look at this because I would say, Mr. Chairman, that I know that there are utilities all over this country on the thin edge. They would far rather have their regulation done by FERC than by the State utility commission in the State in which they reside.

Senator HEFLIN. I am interested in whether there is any legislative history to indicate the role of the State regulatory commissions in the reorganization of a public utility when it is in bankruptcy.

Senator RUDMAN. Well, I would also suggest, Mr. Chairman, that your staff do what we have done and go back and look at those sections which I have stated here in my statement, which there are various sections that I have quoted which talk directly about the powers of States to continue to regulate and so forth, and I think they are very instructive.

Senator HEFLIN. Senator Thurmond, do you have some questions?

Senator THURMOND. I just have one question. Senator Rudman, the Public Service Co. of New Hampshire plan of reorganization places a portion of its rates under the jurisdiction of the Federal Energy Regulatory Commission. I believe that is correct; is it not?

Senator RUDMAN. That is correct. Those would be wholesale rates, Senator Thurmond.

Senator THURMOND. Do you believe that the Federal Energy Regulatory Commission will adequately protect the public interest regarding the approval of any increases in utility rates sold in the future?

Senator RUDMAN. Senator Thurmond, let me say regrettably that the answer is clearly no. And the reason is clearly no is, you know, I have come to the view somewhat reluctantly in this city that the regulators in a variety of areas tend to be far too close to the industries they are supposed to regulate than to the consumers they are supposed to protect. That is the first part of my answer.

The second part of my answer is that under the longstanding federalist principles which we talk about a great deal here, it is inconceivable to me that a utility that has all of its customers in the State of New Hampshire which is the Public Utility of New Hampshire, that is its name—Public Service Co. of New Hampshire—would be able to have its rates set by a Federal body. Now they are going to come and say, well, it is the wholesale rates. That is true. But the retail rates will flow from the wholesale rates, and under no circumstances do we think that the people of New Hampshire would be adequately protected.

Our Public Utilities Commission is appointed by the Governor, confirmed by the executive council. It is responsive to the needs of consumers, but it has been a responsible body over the years. It has in the main discharged its responsibilities very well, even in some very tough cases. So I would point out to Senator Thurmond that I regret to say it, but I have very little faith in the power of Federal regulators to protect individual consumer interests.

Senator THURMOND. Now the Public Service Co. of New Hampshire owns the Seabrook plant, I believe.

Senator RUDMAN. They own a portion of it.

Senator THURMOND. They own a portion of it.

Senator RUDMAN. That is correct. They originally owned a great portion of it. And they have owned less and less, but the power will be used heavily in New Hampshire.

Senator THURMOND. Now who owns the rest of it?

Senator RUDMAN. Other utilities. But, of course, the reorganization—

Senator THURMOND. What percent of the population does this Seabrook plant serve?

Senator RUDMAN. Well, theoretically all of the State would benefit from power from this plant. I have been a supporter of the plant, not a supporter of some of the procedures that have been followed in the last 3 or 4 years, but a supporter generally of nuclear power. I would observe, Senator Thurmond, that it is not just Seabrook we are talking about here. It is the Public Service Co. of New Hampshire which is going to be setting up distributing companies and retail companies and supply companies, a very complicated maneuver here, but the bottom line is they want to get the power rates set down here in Washington. And that is the bottom line, whatever the power source is.

Senator THURMOND. Do you need the power from the Seabrook plant?

Senator RUDMAN. I believe we do.

Senator THURMOND. I understood the State needed it.

Senator RUDMAN. I believe the entire region probably needs additional power. There are some who would disagree.

Senator THURMOND. Now if the Senate does what you are asking the Congress to do, or if the Congress does it, then what effect is that going to have on the Seabrook plant survival?

Senator RUDMAN. Oh, I think it will survive. I simply think that what will happen is that some of those who took great risks in their investments late in the game, knowing that this anti-CWIP law was on the books and knowing that there was a great risk, which is why they were receiving 21 percent interest in some cases, will receive less than 100 percent on the dollar on their investment. In other words, the basic base on which the rate will be calculated will be contracted because of money that will not be flowing back to these people who took the high risk.

They will receive in most cases, I assume, some money, but they were speculators, and speculators, I assume, take some risks.

Senator THURMOND. In other words, you think the Seabrook company can survive and make a fair rate of profit on the investment?

Senator RUDMAN. No question in my mind that, in fact, will happen, and I believe that Seabrook will open. There are some who would disagree with that statement, or would be unhappy with it. However, I think it will open, and I think it will operate, and I think the people of New Hampshire are going to have very healthy rate increases.

As a matter of fact, we have one of the highest power costs in the country today, and my guess is that over the next 5 years in aggregate, rates will rise—it would not surprise me—in the vicinity of 25 to 40 percent over that 5-year period if we are under present law. If FERC is allowed to set that rate, then I believe that the State of New Hampshire could be paralyzed economically by utility rates that would be so high as to force industries to leave our State.

Senator THURMOND. Thank you, Mr. Chairman.

Senator HEFLIN. Senator Rudman, let me ask you one further question. As I understand, your argument, if this bill is not passed, then FERC, in effect, sets the wholesale rate, and that therefore the state regulatory agency has no alternative but to pass that portion of the wholesale rate on to the consumer, to the ratepayers.

Senator RUDMAN. That is absolutely correct. That is the present law.

Senator HEFLIN. You say present law.

Senator RUDMAN. We presently have power that comes into the State of New Hampshire that Public Service may buy from other utilities that is regulated by FERC. And we understand that, but this is not their prime generating source.

Senator HEFLIN. Well, is it within the domain of your State legislature to amend the law in a manner which there is not an automatic pass on?

Senator RUDMAN. I do not believe so, Mr. Chairman. I think you are getting into interstate commerce now, and I think you have got some Federal legislation involved there. I do not think you could do that.

Senator HEFLIN. You do not think it is within the domain of the State legislature to, in effect, decide how much of the wholesale rate to press on the the ratepayers?

Senator RUDMAN. I do not believe the State legislature in New Hampshire could pass legislation that would be constitutional, essentially saying that the State Utilities Commission could disregard a properly set wholesale price set by a Federal regulatory agency that was established pursuant to a legislative scheme of the United States. No, I do not think so.

Senator HEFLIN. Thank you. We appreciate your testimony.

Senator RUDMAN. Mr. Chairman, Senator Thurmond, thank you.

Senator HEFLIN. Next, we have Mr. John P. Arnold, the attorney general of the State of New Hampshire, accompanied by Mr. Larry Smuckler and Mr. Norman Stahl. Mr. Mark Vaughn is also present. Mr. Arnold, we would be delighted to hear from you.

PANEL CONSISTING OF JOHN P. ARNOLD, ATTORNEY GENERAL, STATE OF NEW HAMPSHIRE, CONCORD, NH, ACCOMPANIED BY LARRY SMUCKLER, ASSISTANT ATTORNEY GENERAL, STATE OF NEW HAMPSHIRE; NORMAN STAHL, ESQ., DEVINE, MILLIMET, STAHL & BRANCH, MANCHESTER, NH; AND MARK W. VAUGHN, ESQ., DEVINE, MILLIMET, STAHL & BRANCH, MANCHESTER, NH

STATEMENT OF JOHN P. ARNOLD

Mr. ARNOLD. Good morning, Senators. I am John P. Arnold, attorney general of the State of New Hampshire. I wish to thank the members of the subcommittee for inviting me to address you today. Sitting with me are members of the state legal team in the Public Service Co. of New Hampshire bankruptcy: Senior Assistant Attorney General Larry M. Smuckler; Norman Stahl and Mark Vaughn from the firm of Devine, Millimet, Stahl & Branch, the State's special bankruptcy counsel.

The legislation before you is of vital importance to the State of New Hampshire. It is also important to those States where in the absence of this legislation electric utilities may resort to the Bankruptcy Code to circumvent unfavorable State regulatory rulings. This danger is particularly acute given the elimination of the insolvency requirement for chapter 11 protection.

As you may know, the U.S. Supreme Court has recognized that, and I quote:

The regulation of utilities is one of the most important of the functions traditionally associated with the police power of the States.

Such regulation is implemented by a regulatory compact that grants electric utilities monopoly power to service captive customers in exchange for being subject to State regulation. In fact, it is the oversight of a comprehensive regulatory system that exempts these monopolies from State and Federal antitrust laws. I will address this matter in the context of the Public Service bankruptcy which brought this issue to our attention, but make no mistake, the issues raised here affect regulatory systems nationwide.

The issue before you is whether an electric utility may continue to enjoy the monopoly benefits of serving captive customers while using the Bankruptcy Code to escape from its regulatory obligations. The view proffered by Public Service would allow just that sort of monopoly abuse to occur. Public Service is an electric utility which services approximately 75 percent of New Hampshire's population. Its actions have a direct and significant effect on the State's entire economy.

It has invested in the construction of the Seabrook nuclear power plant, a facility that itself more than triples Public Service's total electric plant investment. Part of the cost of Seabrook is the result of high financing costs, enhanced rates of return allowed by the New Hampshire Public Utility Commission to provide investors with returns which reflect the fact that New Hampshire's anti-CWIP law allocates construction risk to investors. Although Public Service in its glossy presentation attempts to argue to you that its management was prudent, we believe this question is more appropriately left to the proper regulatory authorities.

New Hampshire law provides that Public Service can seek full recovery of and on its investment at such time as the plant becomes operational. The State at all times has taken the position that we would be satisfied with a Public Service commitment to adhere to State regulatory requirements. If Public Service is able to justify rate recovery to the New Hampshire Public Utility Commission at the appropriate time, it would receive its requested rate relief.

Public Service's refusal to make this commitment and its attempt to evade State regulation through the bankruptcy process belies its rhetorical commitment to the public interest. The bankruptcy process is designed to be an efficient mechanism for protecting a debtor from its creditors.

Unlike the New Hampshire utility regulatory body which has a statutory duty to balance the interest of the parties, the role of a bankruptcy judge is to balance the interest of debtors and creditors. This is appropriate given the continued application of other legal requirements affecting creditors' rights against the debtor that leave the debtor no better and no worse off than other members of the community.

A debtor can certainly enhance the value of its estate if it is free to disregard the criminal and civil system within which it must do business. Indeed, in New Hampshire as in other States, violation of

the public utility code by regulated monopolies is a felony. The continued applicability of these provisions is the proper manner to ensure that monopoly utilities cannot act in derogation of the public interest.

In this context, Mr. Rosen is profoundly mistaken in his testimony when he states that we are seeking to exercise jurisdiction beyond the usual areas of regulatory concern and expertise. S. 46 is designed to preserve the ability of the States to balance investor and public interest in precisely those usual areas of regulatory concern and expertise.

The exercise of State police power to protect the public from monopoly abuses is no more of a veto than police power restrictions against other criminal activities. I would like to address several other issues raised in presentations submitted by Public Service. Public Service claims that the New Hampshire Public Utility Commission will continue to regulate retail rates. While technically correct, the statement misleads by ignoring the real limitations on State authority to refuse to prevent a complete passthrough of FERC-approved wholesale rates, the rates which formed the substantial portion of the cost of electricity.

Indeed, a key area of preemption sought by Public Service in its plan of reorganization is approval of the power purchase contract between the retailer and wholesaler. Public Service believes that once the bankruptcy court approves that contract, the State must require local ratepayers to pay the cost regardless of whether the retailer's decision to enter into that contract was imprudent because of the availability of less expensive wholesale power.

If Public Service really believed that the State regulation would continue to be a viable form of public protection, it would not be engaging in such an intense effort to evade it.

The other issue raised by Public Service is the issue of retroactivity. Public Service claims that it is unfair to change the law retroactively. This claim rests on Public Service's articulated position that S. 46 is a radical change in the Bankruptcy Code. We do not believe that Congress intended in the present Bankruptcy Code to allow electric utilities to abuse monopoly power by preempting State police power regulatory requirements.

Thus, S. 46 is a clarification rather than amendment. In the pending bankruptcy case, the argument before the judge revolves around the intent of Congress. It is not unfair to the court, the parties, regulators, and investors nationwide to pass legislation clarifying congressional intent. Public Service has been able to retain national bankruptcy counsel and lobbyists financed by millions of estate dollars authorized by the bankruptcy judge.

These expensive professionals are certainly competent and able to present the clever arguments reflected in the lengthy glossy statement, arguments which are correct in form but misleading in substance. We must be careful with taxpayers' dollars, but it was necessary for us to come here for ourselves and other States to protect not a parochial or special interest but rather the public interest. In considering this legislation, we ask that you do the same.

My colleagues would be happy to answer any questions which the subcommittee might have.

[The statement of Mr. Arnold and answers to questions submitted by Senator Heflin follow:]

STATEMENT OF ATTORNEY GENERAL OF NEW HAMPSHIRE
BEFORE THE SUBCOMMITTEE ON COURTS AND
ADMINISTRATIVE PRACTICE

S.46, ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT

I wish to thank the members of the Subcommittee for permitting me to address you here today. My name is John P. Arnold. I am the Attorney General of the State of New Hampshire.

The legislation before you is of vital importance to the State of New Hampshire. It is equally important to other states which are or may be confronted with a utility bankruptcy proceeding. This legislation has major significance for this nation in that it reinforces the fundamental balance of our federal system by making clear that state regulatory authority remains in effect for bankrupt public utilities.

I would like to take a moment to outline for you the situation in New Hampshire. New Hampshire's utility laws are by no means unique, and a review of the situation in New Hampshire is very illustrative of what could happen in your own states in the event that this proposed legislation is not enacted.

Public Service Company of New Hampshire, which I will refer to as "PSNH", is a private corporation which is engaged in the

business of providing electric utility service to approximately three-fourths of New Hampshire's population. It enjoys a monopoly on the providing of electric utility service within its service territory by virtue of a franchise granted to it by the New Hampshire Public Utilities Commission. All of its customers are in New Hampshire.

PSNH is for the most part a single integrated electric utility. By that I mean that it is engaged as a single corporation in the generation, transmission and distribution of electric energy. Being organized in this manner, substantially all aspects of its business are regulated by the New Hampshire Public Utilities Commission. This regulatory authority extends not only to the regulation of rates but also to a number of other organizational and financial matters including the issuance of securities, transfers and leases of assets, commencement and termination of electric service, approval of construction plans and many other matters. The types of regulations involved are quite similar to those found throughout the country. In addition, New Hampshire has in place, similar to certain other states, a so-called anti-CWIP statute, which prohibits the reflection in utility rates of costs of new construction until the construction is completed and actually providing service to the public. This statute also prohibits the recovery from ratepayers of the costs of cancelled projects. This New

Hampshire statute was enacted in 1979, and its constitutionality has been upheld by the New Hampshire Supreme Court, and PSNH's appeal of that decision to the United States Supreme Court was denied.

See, Petition of Public Service Company of New Hampshire, 130 N.H. 265, 539 A.2d 263 (1988); appeal dismissed sub nom. Public Service Company of New Hampshire v. New Hampshire ___ U.S. ___, 109 S.Ct. 858, 102 L.Ed.2d 983 (1989). On January 28, 1988, PSNH sought protection from its creditors under Chapter 11 of the Bankruptcy Code. Its financial problems are entirely attributable to its investment in the Seabrook nuclear project located in Seabrook, New Hampshire. This project has been controversial from its inception. It was originally forecasted to cost some \$900 million for two 1,150 megawatt generating units. One of those units has now been cancelled and the commercial operation date of the other is more than a decade behind schedule. Published reports indicate the total cost of the remaining generating unit will be in excess of \$6 billion. PSNH owns approximately 35% of the Seabrook project. The debt service requirements on PSNH associated with its financing of these staggering cost overruns precipitated PSNH's financial collapse.

In 1982 the New Hampshire Public Utilities Commission attempted to assert some level of control over the determination by PSNH to continue with this construction program. However, PSNH was successfully able to persuade the New Hampshire Supreme Court that it had acquired a vested right to complete the Seabrook Plant and that PSNH's decisions with respect to pursuing completion of the Plant were to be left to the sole discretion of management without interference by the Public Utilities Commission. The Court reasoned that since ratepayers were not financing the construction effort, regulatory review would occur when the Seabrook plant began providing electric service. PSNH relied on this decision to continue funding construction regardless of the cost. It issued vast amounts of securities comprised primarily of "junk bonds" in order to finance its share of the construction costs. Some of the debt instruments which were issued to finance this construction carried yields as high as 21% per annum. The New Hampshire anti-CWIP statute had the effect of allocating the entire construction risk associated with Seabrook to investors, and investors were compensated handsomely for assuming this risk.

PSNH has now seized upon some unfortunate draftsmanship within the Bankruptcy Code to impose an after-the-fact reallocation of the construction risk to ratepayers for the sole purpose of increasing the rewards to stockholders and bondholders

of their speculative investment. To do so, PSNH has proposed a plan of reorganization which would split the Company into several separate corporations with the primary purpose of enabling PSNH to evade in large part the New Hampshire regulatory framework. Most importantly, PSNH proposes to split the generation and transmission portions of its business away from the business of actual distributing and selling electricity at retail. These separate corporations would all remain within the umbrella of a single holding company. The effect of this restructuring is to create a situation where the generating company sells electricity to the distributing company. These "wholesale" sales would be made pursuant to a long-term contract with the generating company which the distributing company will be forced to enter into, regardless of the availability of lower cost electricity from other sources. The terms and conditions of this long-term contract, including the rates and charges to be paid by the distributing company under the contract, would be regulated by the Federal Energy Regulatory Commission under the Federal Power Act rather than by the New Hampshire Public Utilities Commission. The reason for doing so is that the current state of regulatory policy by the Federal Energy Regulatory Commission is to allow a portion of construction work in progress ("CWIP") to be recovered in rates before projects are completed and to allow a substantial recovery for cancelled or abandoned plants. The effect is to allow investors who invested in PSNH on the assumption that they

were taking the entire construction risk of Seabrook and who were compensated for that risk to switch to a system that allocates a significant portion of the construction risk to ratepayers in order to receive additional compensation on their investments. This compensation would be paid through the requirement that the retail distributing company pass along to customers all of the costs associated with this FERC-regulated power contract. This reallocation of regulatory jurisdiction would occur even though the entire electric service territory of the distribution company would remain within New Hampshire.

Under New Hampshire law, and the laws of most states are very similar, this corporate restructuring could not take place without approval of the Public Utilities Commission. This restructuring will involve, among other things, the transfer of retail distribution assets to the new distributing company, the granting of an authorization to the new distributing company to operate as a public utility within New Hampshire, the issuance of various securities by all of these utility entities, and the execution of various mortgages. Under New Hampshire law, the PUC is authorized to approve these various transactions in the event that it determines that such approval would be consistent with the public good.

PSNH has taken the position that the Bankruptcy Code authorizes it to implement these transactions without any approval by the Public Utilities Commission and, in fact, without any public interest review at all. The decision of how to allocate construction risk is changed from a matter of state regulation to a matter of federal regulation, not pursuant to a regulatory authority determining that such a reallocation is in the public interest, but solely to change the rules of the game for investors and enhance their profit. We know that if they are right, the implications are profound for New Hampshire. We believe that if they are right, Congress has made a fundamental change in the balance of state and federal authority and granted broad powers for reorganizing entities to disregard non-bankruptcy state and federal laws. People may stand before you today and say that this was your intent in enacting the current bankruptcy laws. I cannot believe that that is the case.

The PSNH argument is premised on the language contained within Section 1123(a) of the Bankruptcy Code, which provides as follows:

"(a) Notwithstanding any otherwise applicable nonbankruptcy law, a plan shall-

* * *

(5) provide adequate means for the plan's implementation such as-

(A) retention by the debtor of all or any part of the property of the estate;

(B) transfer of all or any part of the property of the estate to one or more entities, whether organized before or after the confirmation of such plan;

(C) merger or consolidation of the debtor with one or more persons;

(D) sale of all or any part of the property of the estate, either subject to or free of any lien, or the distribution of all or any part of the property of the estate among those having an interest in such property of the estate;

(E) satisfaction or modification of any lien;

(F) cancellation or modification of any indenture or similar instrument;

(G) curing or waving of any default;

(H) extension of a maturity date or a change in an interest rate or other term of outstanding securities;

(I) amendment of the debtor's charter; or

(J) issuance of securities of the debtor, or of any entity referred to in subparagraph (B) or (C) of this paragraph, for cash, for property, for existing securities, or in exchange for claims or interests, or for any other appropriate purpose;

* * *

PSNH claims that the "notwithstanding" language in the introduction of Section 1123(a) authorizes the proponent of a

reorganization plan to include in the plan anything within the subject matter of the provisions of Section 1123(a) without regard to any other law, state or federal, civil or criminal. If the reorganization plan is approved by the bankruptcy court, PSNH contends that the plan provisions are "self-executing". In other words, upon confirmation, these plan provisions can be implemented in all respects without regard to any other law which by its terms prohibits transactions contemplated within the plan. On this basis, PSNH contends that New Hampshire's regulatory laws which require PUC approval of asset transfers, new utility franchises, issuances of securities, mortgages, etc. are pre-empted and are of no force and effect for a reorganizing electric utility company. PSNH further contends that this result is exactly what Congress intended.

I would point out that the introductory language contained in the Bankruptcy Code as enacted in the Bankruptcy Reform Act of 1978, simply stated that "a plan shall" contain the various mandatory plan provisions. The "notwithstanding" language was enacted as part of a series of "technical corrections" made in the Bankruptcy Amendments and Federal Judgeship Act of 1984. It is fair to say that all parties to the PSNH bankruptcy case have searched diligently for whatever legislative history there is regarding the intent of Congress in the enactment of this language. One thing is clear, there is no statement by any

member of Congress within the legislative history suggesting in any way that Congress intended to displace utility regulation. We believe that this language was inserted to make clear that creditors and equity security holders could not enhance their position by exercising contractual and statutory rights as creditors and equity security holders to block the reorganizing debtor from proposing an equitable reorganization plan. However, the language is ambiguous, and we believe that at least in the electric utility context, it is imperative that the law be clarified.

The State of New Hampshire is pressing its position regarding the appropriate construction of Section 1123(a) before the Bankruptcy Court and will continue to press that position all the way to the Supreme Court of the United States, if that is the course that this proceeding takes. However, in the meantime, due to what we believe is some poorly chosen language within the Bankruptcy Code, the State of New Hampshire will be held hostage, perhaps for years during the course of this litigation, to the prospect of massive rate increases. We believe that massive rate increases could have a severe adverse effect on the economy of the State of New Hampshire. In fact, there are studies indicating that the presence of the risk of massive rate increases is having an adverse effect on the New Hampshire economy at the present time. It is absolutely essential that

Congress clarify the Bankruptcy Code to make clear that state and federal regulatory laws continue to apply to reorganizing electric utility companies. S.46 will take this step and make clear the mandate of Congress that bankrupt public utilities conform to regulatory laws.

I would ask the Subcommittee to keep in mind that we are dealing here with monopoly enterprises which are not favored in the American economic system. In general, the anti-trust laws prohibit the creation and operation of monopoly enterprises. However, historically, it has been determined that for certain types of enterprises providing essential services that the operation of monopoly enterprises is warranted. In these cases, it is regulation which protects the public from the likelihood of predatory practices by profit-oriented monopolies. In a competitive environment, it is the competitive marketplace which exercises control over the prices and practices of business enterprises. In the case of regulated monopolies, regulation is the constraining force where market forces cannot operate. It is this regulatory framework which exempts monopoly utilities from the anti-trust laws. If the PSNH position is correct, not only do we have a situation in which Congress has chosen to override state law, we also have the result that the entire mechanism for protection of the public, namely the public interest review of monopoly transactions, is entirely eliminated. There is no

express provision anywhere in the Bankruptcy Code which requires or authorizes the Bankruptcy Judge to consider the public interest in approving transactions such as this by electric utilities in reorganization plans. PSNH has argued to the Bankruptcy Judge that the presence of such a public interest requirement in other portions of the Bankruptcy Code is indicative of your intent that the public interest be ignored in electric utility bankruptcies. The public interest is not the constraining force. Rather, the nature and effect of the transactions proposed in the reorganization plan are limited only by the imagination of the plan proponent and the economic demands of creditors and equity security holders. As a policy matter, this result would stand in stunning contrast to historic congressional policy with respect to the control of monopolies and deference state regulation of utilities.

I understand that you will also be hearing today from a number of bankruptcy professionals and that some of those professionals will oppose this legislation. This is not surprising to me. Bankruptcy attorneys can be fully expected to ascribe little significance to regulatory policy which is so important to state governments. Bankruptcy professionals quite naturally seek as many tools as can be made available to them to produce favorable results for their respective debtor and creditor constituencies. However, in the context of electric

utilities, the interests of debtors and creditors are not the only ones to be addressed. There is a consuming public out there which is affected by the transactions consummated pursuant to reorganization plans. I would ask you to consider as you hear the comments of each of these professionals, how the public interest is to be protected. Remember, the public will have no vote on the reorganization plan. Its sole protection will come from the regulatory process.

I have seen the glossy presentation prepared by PSNH's lobbyists to be filed with you today. The "General Summary" contains a blatant misstatement that can only have been intended to mislead this Subcommittee. Page 3 of the General Summary states as follows:

"Under the existing Bankruptcy Code, the state public utility commission remains the ultimate gatekeeper to retail rates and the marketplace. No utility -- whether a thriving company or a reorganized bankrupt -- can collect any rates without the approval of the state public utility commission. Thus S.46, while disrupting the structure of the Code, does not in the final analysis vindicate a state's interest in protecting its citizens from unreasonable rates for electric power."

The primary purpose and effect of the PSNH plan is to strip the New Hampshire Public Utilities Commission of authority to determine how the costs of Seabrook, and in general the costs of generating and transmitting electricity, will be reflected in retail electric rates. The purpose of the PSNH plan is to impose

on New Hampshire a structure under which the FERC makes these decisions pursuant to the power contract created under the Plan and the New Hampshire Public Utilities Commission is forced to pass these costs on to retail customers. PSNH's statement to the contrary is a stunning misrepresentation.

There are two additional concepts which we in New Hampshire have heard many times in the course of the PSNH bankruptcy and that we expect you will hear today. These two concepts are "regulatory veto" and "regulatory failure". I would like to take a moment to address each.

First, it is asserted that the State of New Hampshire is seeking to establish for itself a veto of any reorganization plan formulated for PSNH. We object most strenuously to this characterization of the State's position. We have not requested, nor would our position result in, a veto over reorganization plans. The result would be protection of the existing State statutory framework under which the regulatory process after full notice and hearing determines whether transactions covered by the respective statutes will be consistent with the public good. This legislation will preserve a level playing field between utilities which are undergoing bankruptcy proceedings and utilities which are not. It will leave in place, neutral, validly-enacted police power regulations designed to protect the

public from predatory practices by franchised monopoly enterprises while preserving the constitutionally mandated opportunity for investors to earn a reasonable rate of return. We do not believe that the State is exercising a veto over the conduct of utilities any more than it exercises a veto over criminal conduct by its citizens, a veto over environmental pollution and other exercises of authority pursuant to a state's inherent police powers. The State's powers in relation to public utilities are exercised pursuant to a comprehensive regulatory framework with express statutory standards and full due process protections. The State proposes the enforcement of neutral regulatory laws, not a "veto".

The other concept which we expect you will hear is "regulatory failure". PSNH contends that Congress must have intended to displace regulation in reorganization plans of electric utility debtors because in its judgment no utility would be the subject of Chapter 11 proceedings unless the regulatory system had failed. PSNH's premise is faulty both as a generic matter and as applied in this specific case. There are a number of ways in which public utilities can involve themselves in activities which result in economic disaster for which there is no right of indemnification from the utility's customers. For example, financial failure can result from diversified enterprises or, as here, from management decisions to assume the

risks of construction projects, which, to put it mildly, have not turned out as planned. Congress simply has not determined that every utility bankruptcy must be resolved through a federally mandated bailout by ratepayers. With the passage of this legislation, the intent of Congress to preserve the role of state regulatory authorities will be made clear.

I would be pleased to answer any questions that the Subcommittee may have.

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JOHN P. ARNOLD

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August 18, 1989

The Honorable Howell Heflin
Chairman, Subcommittee on Courts
and Administrative Practice
Senate Judiciary Committee
223 Hart Senate Office Building
Washington, D.C. 20510

Re: S. 46, the "Electric Utility Bankruptcy
Clarification Act"

Dear Senator Heflin:

I am writing to respond to the questions transmitted with your letter of August 3, 1989 relating to S. 46, the Electric Utility Bankruptcy Clarification Act. We very much appreciated the opportunity to testify before the Subcommittee and we certainly appreciate your continued consideration of this important legislation.

Our answers to your questions are as follows:

1. Would you explain the role of the State of New Hampshire in the bankruptcy reorganization of Public Service of New Hampshire?

Public Services Company of New Hampshire ("PSNH") is an electric utility company and the monopoly supplier of electricity to three-fourths of the population of the State of New Hampshire. The public is protected from the potential for

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monopoly abuses through the State's utility regulatory process administered by the New Hampshire Public Utilities Commission ("NHPUC"). Under New Hampshire's utility laws, the NHPUC regulates not only the rates charged by PSNH but also the terms and conditions of electric service, the continuation of electric service, safety and reliability of service, the issuance of securities, power supply planning, the purchase of electricity from co-generation facilities and small power production facilities and in a number of other respects all relating to insuring that New Hampshire has a safe and reliable supply of electricity at just and reasonable rates. This role for the State of New Hampshire is no different from the State's role with respect to other public utilities.

The State has also been granted the status of a party in interest under Section 1109(b) of the Bankruptcy Code (11 U.S.C. §1109(b)) and that of a general intervenor pursuant to Bankruptcy Rule 2018(a). See, In re Public Service Company of New Hampshire, 88 B.R. 546 (Bankr. D.N.H. 1988). I would point out that the granting of party in interest and general intervenor status for the State was vigorously contested by PSNH and investor groups. The State's main interest in the bankruptcy proceeding has been to protect the state regulatory process from being overridden in the bankruptcy proceeding. The State has also been very active in defending the regulatory process as it relates to the confirmation and implementation of reorganization plans. The ambiguity under existing law with respect to the extent to which the regulatory process remains in effect during the plan confirmation and implementation process has given rise to substantial litigation. The need for this litigation and this aspect of participation by the State in the bankruptcy proceeding itself would be alleviated by clarification of the relevant bankruptcy code provisions, as is discussed further in the response to Question 2 below.

Finally, the State has been actively engaged in negotiations with all parties in an attempt to fashion a consensual settlement of the bankruptcy case. The uncertainty regarding New Hampshire's energy future that arises from the pendency of this bankruptcy case is a source of concern for the State's economy.

Ultimately, the State's role in the PSNH bankruptcy is to protect the public interest, a role which Congress has not provided for in the bankruptcy process other than in railroad reorganizations. It is this failure to provide for the public

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interest in the Bankruptcy Code which persuades the State that Congress intended to leave intact the non-bankruptcy regulatory processes which are designed to protect the public interest. Those factors go beyond rates and reach all matters relating to the safety and reliability of electric service and transactions which inevitably will drive rates.

2. It has been suggested that S.46 is a mere clarification of the bankruptcy law. But S.46 gives the state regulatory agency expanded authority than currently authorized under the Code. How do you perceive this as a mere clarification?

The State of New Hampshire does not believe that S.46 would as a substantive matter provide state regulatory agencies with more authority than they now have over bankruptcy electric utilities. On the contrary, we believe that Congress intended to leave intact state regulatory processes. Throughout the course of the pending bankruptcy, the provisions of 28 U.S.C. §959(b)¹ and the police power exceptions to the automatic stay provided by 11 U.S.C. 362(b)(4) and (5) have allowed the continued functioning of state regulatory procedures. Furthermore, there has been no determination of Congressional intent to preempt state regulatory processes in the formulation and implementation of reorganization plans. The State has made its arguments forcefully before the Bankruptcy Court in the PSNH bankruptcy case, and a copy of the State's memorandum to that effect is attached hereto as Attachment 1. Unfortunately, introductory language in 11 U.S.C. §1123(a), which was inserted as a "technical correction" of the Bankruptcy Code in 1984, has given rise to arguments on the part of PSNH and its creditor and investor constituencies that Congress intended to displace state

¹ (b) except as provided in section 1166 of title 11, a trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

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regulation in the formulation and implementation of reorganization plans. By way of example, the responsive memorandum of the Creditor's Committee is attached hereto as Attachment 2. The issue addressed in these memoranda is whether the existing text of the Bankruptcy Code is clear on this question of preemption. The State believes that preemption of state law in an area having the importance of the regulation of public utilities can only be accomplished by deliberate and specific action on the part of Congress. Based upon the text of the Bankruptcy Code and the absence of any legislative history indicating a preemptive intent, the State asserts that Congress has not acted to preempt state law. However, as Attachment 2 shows, other parties take the contrary position. It is this ambiguity that needs to be clarified not only for New Hampshire, but for a nation as a whole to preserve the integrity of state regulatory laws and to protect the public interest which is otherwise not provided for in the plan implementation process.

3. Section 1129(6) of the Bankruptcy Code provides in part:

The Court shall confirm a plan only if all of the following requirements are met:

(6) Any governmental regulatory commission with jurisdiction after confirmation of the plan, over rates of the debtor has approved any rate change provided for in the plan ...

If the PUC retains the authority under Section 1129(a)(6), to approve any rate change under the reorganization plan, why is this insufficient to protect ratepayers?

The pervasive regulatory authority granted to utility commissions in all of the states is based on the proposition that the ability to control the price of electricity is not sufficient in itself to protect the public interest. The regulatory authority must also be able to review transactions which will necessarily affect the safety, reliability and cost of utility service. Utility rates are designed to provide utilities with a reasonable return on investment after expenses. The amount of investment in utility property is the utility's "rate base." The return on investment is, at a minimum, the utility's cost of capital. Effective rate regulation necessarily, therefore, must include controls over growth in rate base and controls over financing transactions

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which determine the utility's costs of capital. If such transactions can be consummated without any review into their impact on the safety and reliability of service and on the future costs of electricity, the regulatory authority's ability to act as gatekeeper is severely constrained by the fact that the horse has long since left the corral.

In the particular case of PSNH, confining regulatory authority simply to the review of rates allows the debtor to change completely the structure by which electric utility services are provided in New Hampshire from one involving a single integrated utility corporation to a holding company structure with split functions performed by separate corporations pursuant to contracts over which the State of New Hampshire will have no control. In the case of New Hampshire, this result is quite intentional, with the design being to avoid the impact of the State's so-called "anti-CWIP" law, which precludes construction projects such as Seabrook Station from being reflected in rates unless and until the projects are actually providing service to the public. A restructuring to provide for rate regulation of the generation end of the business by the Federal Energy Regulatory Commission results in an ability to alter this basic balance between investors and ratepayers by taking advantage of FERC rules which in certain circumstances allow for the inclusion of CWIP in rate base and for recovery of certain cancelled plant costs. The effect of this regulatory change is to allow investors, who purchased their investments in the anti-CWIP environment and were paid high returns reflecting that environment to remove the risks for which they have been compensated. Under the view of the law espoused by PSNH and its creditors and investors, this structural change can be implemented without a public interest review by state regulatory authorities through a confirmation order by the Bankruptcy Court, which in their minds as well, would include no public interest review.

In sum, the confining of regulatory review to ultimate rates of the debtor provides a franchised monopoly corporation which provides essential services with the opportunity to engage in manipulative and predatory practices for economic gain without regard to the impact on the public.

4. How do you respond to the criticism that S.46 gives the state regulatory agency the power to veto a plan of reorganization, which undermines the ability of the Bankruptcy Code to work out an acceptable plan of reorganization?

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The State of New Hampshire does not seek a "veto" over a reorganization plan any more than the Environmental Protection Agency is granted a "veto" over the operations of American businesses. Like the EPA, the State seeks to enforce neutral, validly-enacted police power laws. These laws are the same laws that apply to public utilities that are not undergoing reorganization.

It may well be that a monopoly enterprise which can ignore state police power laws is more valuable and, therefore, more readily reorganized. However, it is bad policy to allow basic decisions that will affect the provision of essential services to be made by profit-oriented investors in monopoly enterprises without any review by state regulatory authorities charged with protection of public interest. In fact, it is the very fact that such monopoly actions are subject to state review that exempts such monopolies from federal anti-trust laws.

Furthermore, the State's regulatory process provides specific statutory and judicial standards for agency conduct and full due process protections for affected parties through the State's Administrative Procedures Act. The enforcement of an elaborate regulatory process which provides full due process to affected parties cannot be legitimately characterized as a "veto."

5. The retroactive application of this legislation to pending cases, specifically the Public Service of New Hampshire bankruptcy, is seen by many as an unnecessary intrusion by Congress in a matter that is properly before the Bankruptcy Court. Why should Congress intervene in this particular instance?

This case is not the typical bankruptcy law problem relating to the relative rights and obligations of private civil litigants with respect to their individual economic interests. There are a number of special circumstances which warrant Congress' intervention in this instance.

(a) State-Federal relations. First of all, this case involves the interrelationship between the federal bankruptcy power and the traditional role of the states in regulating intrastate public utility companies. The United States Supreme Court has stated that "... the regulation of utilities is one of the most important functions traditionally associated with the police power of the States." Arkansas Electric Cooperative v.

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Arkansas Public Service Commission, 461 U.S. 375, 377 (1983). Federal courts have traditionally expressed reluctance to interfere with state regulatory processes. In fact, a separate abstention doctrine has been developed in the federal courts as a result of this policy. See Burford v. Sun Oil Co., 319 U.S. 315 (1943). Congress itself has traditionally accorded great deference to state regulation in fashioning federal legislation as is pointed out at length in the State's Memorandum of Law (Attachment 1, pp. 57-62). This factor alone would justify Congressional intervention.

(b) Protection of the public interest. The state interest that will be preserved with the passage of this legislation is in protection of the consuming public from abuses by monopoly enterprises. In the case of electric utilities, the reorganization plan process under the Bankruptcy Code contains no express provision for protection of the public interest. The approach taken by PSNH and the Committees, by design, would result in a structure of approval by the Bankruptcy Court without consideration of the public interest. The Bankruptcy Code provides the public with no vote with respect to the confirmation of an electric utility's reorganization plan. The voice of the consuming public is represented by the regulatory process, and PSNH and its investors have quite cleverly devised a scheme to silence that voice through their interpretation of an ambiguous provision within Section 1123 of the Bankruptcy Code.

(c) Clarification and affirmation of Congressional intent. The purpose of this legislation is to clarify the Bankruptcy Code, not effect a substantive change in the law. The introductory phrase in Section 1123(a), which is the basis for the preemptive interpretation asserted by PSNH, was enacted by Congress without debate as one of a number of "technical amendments" to the Bankruptcy Code in 1984. There is not one shred of evidence in the legislative history to suggest that Congress ever intended through these "technical corrections" to implement a major shift in the state-federal balance as it relates to the regulation of electric utilities. On the contrary, the State of New Hampshire is firmly convinced that if the legal proposition now advanced by PSNH and its investor groups had been brought to the attention of Congress and subjected to debate, it would never have passed. The fact is that members of Congress were never made aware of this potential outcome of the ambiguous language adopted in 1984. This need to clarify the language of the Bankruptcy Code to head off a

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potential interpretation that is contrary to the intent of Congress is an additional compelling reason for Congressional intervention.

(d) Non-interference with settled expectations. The reason for providing for prospective application of statutes is to limit interference with valid settled expectations based on prior law. Such a reason is inapplicable in this instance. Prior to the PSNH bankruptcy, the one area of general agreement was that there exists a high degree of uncertainty as to how the issues arising in a Chapter 11 reorganization would be resolved. Investors simply did not invest in reliance on a clear interpretation of the bankruptcy laws. Rather, the junk bonds were purchased by investors based on a wager that Seabrook would operate in a timely manner. Therefore, S. 46 does not disturb reasonable settled expectations.

(e) Permitted by Constitution. Finally, it is clear that the Constitution does not prohibit prospective legislation. In that regard, reference is made to the case of Matter of Reynolds, 726 F.2d 1420 (9th Cir. 1984), in which constitutional challenges to the immediate effectiveness of a bankruptcy amendment were rejected. A copy of this case is attached as Attachment 3. In fact, this case states the general rule that the law in effect at the time of decision is the law that governs unless Congress clearly states otherwise. Therefore, the provisions of the proposed legislation regarding immediate effectiveness are clearly constitutional.

6. What is the current status of the bankruptcy litigation? If in fact the parties are to reach a consensus, would such an agreement circumvent the need for this legislation?

The bankruptcy litigation involving PSNH has recently passed a major milestone. All of the major constituencies have agreed to proceed on the basis of a rate plan which had been fashioned by the State of New Hampshire and one of the plan proponents, Northeast Utilities. While much remains to be done, and unforeseen factors may intervene, it appears that major rate litigation may have been averted. In specific terms, the court has adopted a procedural schedule calling for all proposed reorganization plans and supporting disclosure statements to be filed on or before September 15, 1989, with hearings on the adequacy of disclosure statements to be completed on or before

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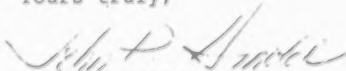
November 15, 1989 and plan consummation to be targeted for completion on or before July 1, 1990.

Therefore, ground work has been laid by which a consensual plan may be developed. The schedule also provides for orderly litigation in the event that no single consensual plan emerges.

Nonetheless, the occurrence of these significant events does not in any way obviate the need for this legislation. State regulatory authorities throughout the nation are at risk as long as the ambiguous language of 1123 is not clarified. In recent years, unfortunately, there have been several electric utility bankruptcies due to a variety of factors. Recently, more electric utilities have come under financial strain. It is apparent that Congress simply did not think about electric utilities in 1978 or in the technical corrections of 1984. The current state of the law is intolerable from the perspective of the public interest. The economic circumstances are such that Congress must think about electric utility bankruptcies and adopt specific legislation which will ensure that regulatory agencies will continue to be able to perform their duties of protecting the consuming public. One thing that the State of New Hampshire has learned from this entire ordeal is that creditors and equity security holders are interested in value available on the date of confirmation and not the economic well-being of customers served by utility customers. The consuming public deserves more, and this legislation will provide it.

I hope that you will find our answers responsive to your questions. If you desire further clarification or if there are other questions, please do not hesitate to ask.

Yours truly,


John P. Arnold
Attorney General

JPA:ab

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW HAMPSHIRE

Attachment 1
FILE COPY

IN RE: PUBLIC SERVICE COMPANY
OF NEW HAMPSHIRE a/k/a
"Public Service of New Hampshire"
"PSNH"
"New Hampshire Yankee"

CHAPTER 11
BK #88-43

HEARING:

JUNE 30, 1989
AT 9:30 A.M.

Debtor

PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE

Plaintiff

v.

THE STATE OF NEW HAMPSHIRE

AND

THE STATE OF NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION

Defendants

ADVERSARY PROCEEDING NO. 89-08

MEMORANDUM OF DEFENDANTS IN OPPOSITION
TO MOTION FOR SUMMARY JUDGMENT AS TO
PREEMPTION OF STATE REGULATORY LAWS

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1989
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U.S. DISTRICT COURT
DISTRICT OF NEW HAMPSHIRE

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UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW HAMPSHIRE

IN RE: PUBLIC SERVICE COMPANY
OF NEW HAMPSHIRE, a/k/a
"Public Service of
New Hampshire"
"PSNH"
"New Hampshire Yankee"

CHAPTER 11
BK #88-43

Debtor.

PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE

v.

THE STATE OF NEW HAMPSHIRE
AND
THE STATE OF NEW HAMPSHIRE PUBLIC UTILITIES COMMISSION

ADVERSARY NO. 89-08

MEMORANDUM OF THE STATE OF NEW HAMPSHIRE
IN OPPOSITION TO MOTION FOR SUMMARY JUDGMENT
AS TO PREEMPTION OF STATE REGULATORY LAWS

Introduction

This memorandum is submitted on behalf of the State of New Hampshire (the "State") in opposition to the motion by Public Service Company of New Hampshire, Debtor-in-Possession (the "Debtor" or "PSNH"), for summary judgment in this adversary proceeding. In its motion, PSNH is seeking a ruling by this Court that:

the Bankruptcy Code and related statutes, including 11 U.S.C. § 1123(a)(5) and 28 U.S.C. § 1334(d), grant the Bankruptcy Court and the proponent of a plan under chapter 11 of the Bankruptcy Code the power and authority to propose, confirm, and implement a chapter 11 reorganization plan of Public Service Company, providing for the transfer or mortgage of property, the

issuance of securities, the acquisition of securities, and other appropriate transactions, without the approval of the New Hampshire Public Utilities Commission (the "NHPUÇ"); whose approval would be required for such transactions outside of the context of proposal, confirmation, and implementation of a chapter 11 plan.

Court Paper No. 1634, at 1. The State has objected to the PSNH motion and requested the Court to enter judgment in favor of the State.

PSNH is a public utility organized under the laws of the State of New Hampshire. It is the exclusive provider of electricity to approximately three-fourths of New Hampshire's population. The consuming public is protected from the potential abuse of monopoly power by the existence of an effective regulatory framework at the state and federal level, the primary purpose of which is protection of the public interest. PSNH and the official committees of the unsecured creditors and equity security holders (collectively, the "Committees") ask this Court to conclude that except as to the rates to be charged by the Debtor, Congress has made a deliberate determination to disregard the public interest in the proposal, confirmation and implementation of plans of reorganization. The State will demonstrate that the only conclusion which this Court can reach on the basis of the text of the Bankruptcy Code, legislative history, and case law is that the State regulatory provisions designed to protect the public interest were left fully intact by Congress in the reorganization process. Accordingly, the

reorganization plan proposed by PSNH, premised as it is on the consummation of various transactions without regulatory approval, contains provisions which are prohibited by law, and on its face the plan is unconfirmable.

Factual Background

PSNH, as a regulated utility, is subject to plenary regulation by the New Hampshire Public Utilities Commission ("NHPUC"). It engages in the electric utility business pursuant to franchise rights granted to it by the NHPUC pursuant to N.H. R.S.A. §374:22-26. The effect of the franchise rights is to permit PSNH to operate as a monopoly providing essential services to the public. In the absence of competition as the prime determinant of prices, PSNH is regulated by the NHPUC as to the rates which PSNH is allowed to charge customers. The NHPUC regulates transactions which affect rates and the quality of service. In fact, substantially the entire relationship between the customer and PSNH is regulated by the NHPUC, including rules regarding the establishment and discontinuance of service, and the actual physical requirements associated with the connection of customers to the PSNH electrical system.

The rates charged by PSNH to its retail customers (sales other than for resale) are exclusively regulated by the NHPUC. PSNH is allowed to earn a reasonable return, after expenses, on

the costs of facilities used and useful in providing service to the public. The costs associated with unfinished or cancelled construction projects cannot be included in rates. N.H. R.S.A. §378:30-a. This statutory feature has been a component of New Hampshire law since 1979, and its constitutionality, both facially and as applied, has been judicially upheld. See Petition of Pub. Serv. Co. of N.H., 130 N.H. 265, 539 A.2d 263 (1988), appeal dismissed sub. nom. Public Serv. Co. of N.H. v. New Hampshire, __ U.S. ___, 102 L.Ed.2d 983 (1989).

As to the transmission of electricity in interstate commerce and with respect to sale of electricity for resale, PSNH is subject to the regulation of the Federal Energy Regulatory Commission ("FERC"). The provisions regarding the determination of rate levels by FERC are substantially similar to those utilized by the NHPUC except for two significant differences. FERC has in effect policies which can allow for the inclusion of up to fifty percent of construction work in progress in rate base and which can provide in appropriate cases for recovery of up to fifty percent of prudently incurred costs associated with cancelled plants.

It is this distinction between the two regulatory systems that is the motivation behind PSNH's plan and this adversary proceeding. PSNH has made a substantial investment in a nuclear electric generating project known as Seabrook Station in

Seabrook, New Hampshire ("Seabrook"). . PSNH is the owner as tenant in common of an ownership share of approximately thirty-five percent of Seabrook. Seabrook has been under construction since 1976. It has never operated, and until certain regulatory issues are resolved in its favor, if ever, it will not operate. Until it does, none of its costs are includable for ratemaking purposes in New Hampshire retail rates.

PSNH, through a series of transactions which it acknowledges would require regulatory approval outside of bankruptcy, is attempting in its plan to reorganize into a structure in which the costs associated with the power generation and transmission functions of its business, including Seabrook costs, would be subject to recovery through FERC-approved wholesale rates. It proposes to do so by forming a public utility holding company, the subsidiaries of which will be a generation and transmission company ("Reorganized PSNH"), a distribution company ("DISCO"), and a service company. It is contemplated that DISCO will be forced to enter into a contract with Reorganized PSNH to purchase its full requirements from Reorganized PSNH regardless of whether more economic power supply arrangements could be made elsewhere. The service company subsidiary will enter into contracts with the other subsidiaries free from regulatory oversight.

PSNH acknowledges that but for the preemption it attributes to Congress in the enactment of the Bankruptcy Code, as amended,

a number of the transactions proposed would require approval of the NHPUC under New Hampshire law. While there may be additional New Hampshire approvals required, and the State reserves all of its rights with respect thereto, the focus of this proceeding is not the adjudication of which approvals are required but whether PSNH is relieved from obtaining these approvals.

The plan submitted by PSNH also seeks to bypass other regulatory requirements. For example, approvals are required under the Federal Power Act, 16 U.S.C. §791 et seq., the Atomic Energy Act of 1954, 42 U.S.C. §2011 et seq., and the Public Utility Holding Company Act of 1935, 15 U.S.C. §79a-z (the "1935 Act"). These federal requirements likewise remain applicable irrespective of the PSNH bankruptcy. PSNH should not be permitted to form a holding company for the purpose of depriving the NHPUC of the major portion of its regulatory authority and then rely on the "intra-state" exemption under section 3(a)(1) of the 1935 Act, which is premised on the effectiveness of state regulation. See 15 U.S.C. §79c(a)(1). PSNH is not entitled to vitiate State involvement in the establishment of the DISCO monopoly while claiming a "state action" exemption from the federal antitrust laws based on "active state supervision." See Patrick v. Burget, 486 U.S. ___, 100 L.Ed.2d 83 (1988), California Retail Liquor Dealers Ass'n v. Medical Aluminum, Inc., 445 U.S. 97, 63 L.Ed.2d 233 (1980), Parker v. Brown, 317 U.S.

341, 87 L.Ed. 315 (1943). Moreover, PSNH is not legally entitled to the relief it intends to seek at FERC in terms of the availability to it of the rules pertaining to the inclusion of construction work in progress in rate base or the recovery of abandoned plant. Further, no ruling by the FERC with respect to the rates to be charged by reorganized PSNH to DISCO will prohibit the NHPUC from examining the prudence of DISCO's choice of generation suppliers and setting rates based on prudent purchasing practices.¹

Finally, as all of the foregoing demonstrates, and on the basis of the presence of other plans of reorganization which would not entail the preemption proposed by PSNH, the State reserves all of its rights with respect to its position, asserted in its motion for interlocutory appeal to the United States District Court for the District of New Hampshire, that adjudication of this motion is not ripe.

1/ For a thoughtful article on the interrelationship of wholesale and retail rate jurisdiction, see Vince & Moot, Federal Preemption Versus State Utility Regulation in a Post-Mississippi Era, 10 Energy L.J. 1 (1989).

SUMMARY OF ARGUMENT

This case raises significant issues of statutory construction and federal preemption of fundamental state interests. These issues are resolvable by a "holistic" review of the Bankruptcy Code, as enacted by Congress, rather than by the strained interpretations and constructions manufactured by PSNH and the Committees. Section 1123(a)(5) of the Bankruptcy Code imposes an obligation upon a plan proponent. That obligation is to include within the contents of the plan "adequate means" for the implementation of the plan. Section 1123(a)(5) contains no provision authorizing the plan proponent to utilize these "means" to disregard valid state and federal police power laws in the confirmation and implementation of the plan. Congress enacted sections 1129, 1141, and 1142 to resolve these issues.

PSNH and the Committees base their arguments upon a faulty premise; namely, section 1123(a)(5) is a self-executing provision. In advancing this premise, PSNH and the Committees ignore several relevant sections of Chapter 11. By ignoring those sections, PSNH and the Committees propose a result that is inconsistent with the explicit statutory language in Chapter 11.

A review of the plan process, from proposal to implementation as enacted by Congress, compels this Court to reject the relief requested by PSNH and the Committees. Section 1121 establishes the standing to propose a plan. Section 1122 delineates the

classifications of claims or interests within which plan proponents may create. Section 1123, captioned "Contents of a Plan", delineates the mandatory and discretionary provisions contained in a plan. Sections 1124, 1125, 1126, 1127 and 1128 define the process under which a plan is prepared for and considered by holders of claims or interests. Section 1129 sets forth the factors which this Court must consider in determining whether a plan may be confirmed. The Court must determine that the plan complies with the Bankruptcy Code, has been proposed in good faith and by means not forbidden by law, and satisfies certain voting requirements. Section 1129(a)(6) constitutes the feasibility pre-requisite for a regulated utility. Without a determination of rates, a plan based on assumed rate levels cannot be confirmed.

Congress enacted sections 1141 and 1142 of the Bankruptcy Code as the statutory effect of confirmation. Significantly, a confirmed plan affects claims and interests only. The plan proponent may implement the confirmed plan, notwithstanding any otherwise applicable law relating to financial condition.

Moreover, the predecessors to the Bankruptcy Code, various proposed amendments and recommendations, and legislative history substantiate a "holistic" view of the Bankruptcy Code and, thereby, mandate a rejection of the arguments propounded by PSNH and the Committees. PSNH and the Committees must struggle to

implant teeth into section 1123 and yet they cannot cite a single piece of legislative history which supports a complete disruption of the established regulatory process. Surely Congress, its subcommittees, or its specially created commission would have discussed some type of preemption in proposing the Bankruptcy Code if section 1123(a) was to have the effect suggested by PSNH. In fact, several proposals, if enacted, would have produced the result now urged by PSNH and the Committees. However, Congress rejected each of these proposals.

The plain language of the Bankruptcy Code, the legislative history, prior statutes, and the recognized fundamental interests of the State in utility regulation warrant only one conclusion. To grant the relief requested by PSNH and the Committees requires an analysis without consideration of the entire framework enacted by Congress. As the State demonstrates in this memorandum, Congress did not empower a plan proponent to obviate legitimate and fundamental public interests.

Finally, a ruling in favor of PSNH nullifies several sections of the Bankruptcy Code and empowers a plan proponent to avoid any state or federal law in the guise of "adequate means" for implementing a plan. The ramifications of the arguments propounded by PSNH and the Committees are bounded only by the imagination of a plan proponent. This Court must question what limits remain if a plan proponent maintains that a particular

provision of a plan constitutes "adequate means" even if that provision violates legitimate and fundamental state laws. In this light, the answer to the question propounded by PSNH is apparent. As is demonstrated in this memorandum, the fundamental rights and interests of the State in regulating a public utility remain in effect during the Chapter 11 process, from the commencement of the proceeding through implementation of the plan.

ARGUMENT

I. THE TEXT OF THE BANKRUPTCY CODE DEMONSTRATES THAT CONGRESS LEFT INTACT STATE POLICE POWER LAWS AND REGULATIONS IN THE CONFIRMATION AND IMPLEMENTATION OF PLANS.

PSNH and the Committees are requesting this Court to rule that Congress, in enacting the Bankruptcy Code in 1978, determined to override all state laws (and federal non-bankruptcy laws) with respect to the formulation, confirmation and implementation of reorganization plans. Furthermore, these parties are asking the Court to accept that Congress chose not just to subordinate state interests to federal interests, but that Congress chose for regulated enterprises such as PSNH to provide for their reorganization in total disregard of the public interest. In support of this proposition, PSNH and the Committees ask the Court to rely on the "plain language" of the Bankruptcy Code contained within section 1123(a) as the evidence that Congress took this step in 1978, even though the language itself did not appear until 1984. Over forty years ago Justice Frankfurter aptly noted that "the notion that because words of a statute are plain, the meaning is also plain, is merely pernicious oversimplification." United States v. Monia, 317 U.S. 424, 431, 87 L.Ed. 376, 382 (1943) (Frankfurter, J. dissenting). The wisdom in Justice Frankfurter's words is no more evident than in this proceeding.

In taking language relating to the contents of reorganization plans and attributing its reach to the confirmation and implementation stages of reorganizations, PSNH and the Committees suggest that reorganization courts have boundless powers to ignore police power restrictions on the conduct of reorganizing enterprises. Furthermore, these parties suggest that the Court's only concern in connection with the exercise of this boundless power is in the implementation of a successful reorganization. It may well be that an enterprise which is free from the constraints of regulatory and criminal laws that govern the balance of society is more valuable and therefore more readily reorganized. However, reasoned analysis of the Bankruptcy Code and its legislative history demonstrates that Congress granted no such license to reorganizing entities.

In the Bankruptcy Code, as enacted in 1978 and as now amended, Congress set out in Chapter 11 to provide for the appropriate treatment of the interests of creditors and equity security holders in failed enterprises. As is demonstrated by the statutory provisions relating to the plan process, Congress did not set about usurping the legitimate exercise by the states and the federal government of valid police power laws.

Sections 1121-1146 of the Bankruptcy Code contain the provisions relating to the proposal, confirmation and implementation of reorganization plans. The statutory structure

and its meaning is best understood by examining all of the relevant sections and analyzing how they interrelate. See United Savings Assoc. of Texas v. Timbers of Inwood Forest Assocs., 484 U.S. 365, ___ 98 L.Ed.2d 740, 748 (1988) (construction of the Bankruptcy Code is a "holistic" endeavor).

After setting forth who may file a plan in section 1121, section 1122 provides for the classification of claims or interests, thereby identifying which parties are affected by reorganization plans and establishing a reasoned basis for distinguishing their treatment under plans. The interests of regulatory authorities are not discussed.

Section 1123 sets forth the mandatory and permissive contents of a reorganization plan. In the form enacted in 1978, section 1123(a) did not contain the "notwithstanding any otherwise applicable non-bankruptcy law" provision relied upon by PSNH and the Committees. Section 1123(a)(5)(B) simply provided that "a plan shall...provide adequate means for the plan's execution such as...transfer of all or any part of the property of the estate to one or more entities, whether organized before or after the confirmation of such plan...." Former 11 U.S.C. §1123(a)(5)(B). Thus, the 1978 version of the Bankruptcy Code contained no language purporting to affect state and federal regulatory laws.

In 1984, as part of the Bankruptcy Amendments and Federal Judgeship Act, Congress amended section 1123 to its current form,

which provides that "(a) notwithstanding any otherwise applicable non-bankruptcy law, a plan shall (5) provide adequate means for the plan's implementation such as [several listed items]." 11 U.S.C. §1123(a)(5). Very little legislative history is available regarding this change. If the addition of this language were to accomplish the usurpation of all non-bankruptcy state and federal laws pertaining to reorganized companies, then one would expect at least a few words of discussion on the subject from Congress. No such discussion exists. Rather, what appears is the conclusion that Congress simply intended to prescribe that the provisions of section 1123 would govern what matters would be required within reorganization plans. H.R. Rep. 1195, 96th Cong., 2d Sess. 22 (1980) ("this amendment makes it clear that the rules governing what is to be contained in the plan of reorganization are those specified in this section[.]").² See

2/ The 1984 amendment to section 1123 was introduced as early as the 96th Congress. Section 102(a)(1) of S. 658, 96th Cong., 2d Sess. (1980), as reported by the House Judiciary Committee, contained the proposed amendment verbatim. The bill was entitled "An Act to correct technical errors, clarify and make minor substantive changes to Public Law 95-598 [the Bankruptcy Code]." H.R. Rep. 1195, 96th Cong., 2d Sess. 22 (1980).

The section 1123(a) amendment appeared again in section 102(a)(1) of S. 863, 97th Cong., 1st Sess. (1981). This bill was entitled "A bill to establish a uniform law on the subject of bankruptcies." The Senate Report accompanying this bill stated very briefly with respect to section 102(a) that "Paragraphs (1) through (5) make technical stylistic changes."

The subject language appeared again in at least two of the many bills on bankruptcy introduced during the 98th (Footnote 2 continued on next page)

also In re FCX, Inc., 853 F.2d 1149, 1154 n.7 (4th Cir.

1988) (amendment to section 1123 did not effect a substantive change).

The only reasonable conclusion regarding the sweep of the introductory language of the current version of section 1123 is that it was intended to avoid the application of contractual and other non-bankruptcy law rights of creditors and equity security holders to prevent the inclusion of methods to resolve equitably their conflicting claims through the distribution of value under reorganization plans. For example, corporate laws prescribing stockholder votes for plans of dissolution, merger, and sale of assets outside of the ordinary course of business could be read to provide an opportunity for equity security holders to exercise powers of corporate governance to block the submission of reorganization plans that did not serve their interests. It is clear that the rights of equity security holders are affected by section 1123, and section 1123 prescribes the contents of plans notwithstanding corporate governance provisions.

(Footnote 2 continued from previous page)

Congress. At section 706(a) of S. 1013, 98th Cong., 1st Sess. (1983), no reference is made to the amendment in the accompanying committee report. Likewise, it appeared at section 405(a) of S. 445, 98th Cong., 1st Sess. (1983). The committee report characterized the amendment to section 1123(a) as a "technical stylistic change."

The amendment to section 1123(a) was incorporated into H.R. 5147, 98th Cong., 2d Sess. (1984), the bill which was ultimately enacted as the Bankruptcy Amendments and Federal Judgeship Act of 1984.

The "notwithstanding" language of section 1123 is limited in its effect to the overriding of limitations of what debtors can include within plans of reorganization. It says nothing about what entities are bound by plans of reorganization, what the effect of confirmation is on entities, and what powers a reorganizing entity has to implement a reorganization plan. Those matters are handled in separate sections of the Bankruptcy Code, and it is clear that those sections do not contain the power claimed by the Debtor and the Committees.

Section 1124 of the Bankruptcy Code provides a standard for determining whether or not claims or interests have been impaired. No mention is made as to the effect of plans on regulatory authorities or the police powers of states and the federal government.

Section 1125 of the Bankruptcy Code governs the process of disclosure and solicitation of acceptances of reorganization plans. No notice is expressly prescribed to regulatory agencies that may be affected by reorganization plans. No opportunity for comment by regulatory agencies is expressly provided. The solicitation is made to the holders of claims and interests.

Section 1126 of the Bankruptcy Code contains the provisions relating to the acceptance of a plan. No role is expressly provided for the acceptance of plans by regulatory authorities.

Section 1127 provides for the modification of plans and section 1128 prescribes a confirmation hearing.

Section 1129 pertains to the confirmation of plans. It provides thirteen requirements, all of which must be met in order for a plan to be confirmed. Two of those requirements are of particular import to this discussion.

First, section 1129(a)(3) requires that "...[t]he plan has been proposed in good faith and not by any means forbidden by law." 11 U.S.C. 1129(a)(3). A plan which willfully transgresses state and federal police power statutes and regulations is as a matter of law not proposed in good faith and is proposed by means forbidden by law. The State recognizes that there are cases to the effect that this section relates to the process of solicitation of acceptances of plans.³ However, that process is fully governed by section 1125, and therefore would be subsumed within the requirements of sections 1129(a)(1) and (2) requiring the plan and its proponent to comply with applicable provisions of Title 11. PSNH's plan contemplates willful violations of regulatory statutes, which constitute criminal offenses in New Hampshire. PSNH identifies a series of transactions to be

3/ Compare In re Wiggles, 7 B.R. 378 (Bankr. N.D. Ga. 1980) ("forbidden by law" means that the proposal of the plan shall not violate any criminal or civil law, including fraud") with In re Acequia, Inc., 787 F.2d 1352 (9th Cir. 1986) (answering an argument that substantive plan provisions were "forbidden by law" by concluding that the plan was consistent with state law).

consummated in the face of specific statutory provisions mandating that certain transactions not be effected without NHPUC approval. New Hampshire law provides the following penalties for taking such actions without NHPUC approval:

Penalty Against Utility. Any public utility which shall violate any provisions of this title, or fails, omits or neglects to obey, observe or comply with any order, direction or requirement of the commission, shall be guilty of a felony and, shall be subject to a civil penalty, as determined by the commission, not to exceed \$25,000. No portion of any fine, nor any costs associated with an administrative or court proceeding which results in a fine pursuant to this section, shall be considered by the commission in fixing any temporary, permanent, or emergency rates or charges of such utility.

Penalty Against Agent. Every officer and agent of any such public utility who shall wilfully violate, or who procures, aids, or abets any violation of this title, or who wilfully fails to obey, observe, and comply with any order of the commission, or procures, aids or abets any such public utility in its failure to obey, observe, and comply with any such order or provision, shall be guilty of a misdemeanor and, shall be subject to a civil penalty, as determined by the commission, not to exceed \$10,000 for each violation, or for each day of a continuing violation.

N.H. R.S.A. §§365:41 & 42. PSNH is clearly proposing to take actions which are "forbidden by law."

The provisions of section 1129(a)(3) go beyond those that were contained in Chapters X and XI of the Bankruptcy Act. section 221(3) of the Bankruptcy Act provided for the following as one of the prerequisites for confirmation:

The proposal of the plan and its acceptance are in good faith and have not been made or procured by means or promises forbidden by this Act.

Section 363(4) of the Bankruptcy Act contained similar language with respect to Chapter XI plans of arrangement. The language of the Bankruptcy Act is in stark contrast to section 1129(a)(3), which requires that the plan "has been proposed in good faith and not by any means forbidden by law." 11 U.S.C. §1129(a)(3) (emphasis added). The sweep of the current version in section 1129(a)(3) is broader than that of the comparable provisions in the Bankruptcy Act. 5 Collier on Bankruptcy ¶1129.02 (15th ed. 1988) ("...section 1129(a)(3) is broader than section 221(3) of the Bankruptcy Act to the extent that section 1129(a)(3) requires that the proposal of the plan comply with all applicable law, not merely the bankruptcy law (emphasis added).").

With this mandate of section 1129 that plans be proposed in conformance with law and the absence of any provision in section 1129 relating to the preemption of non-bankruptcy laws, the function of section 1129(a)(6), upon which the Debtor places so much reliance, can readily be seen. Section 1129(a)(6) is a specific feasibility provision relating to public utility debtors, and no more. It requires as a pre-condition to the confirmation of a plan that:

Any governmental regulatory commission with jurisdiction, after confirmation of the plan, over the rates of the debtor has approved any rate change provided for in the plan, or such rate change is expressly conditioned on such approval.

11 U.S.C. §1129(a)(6).

Section 1129(a)(6) does not represent the only legal constraint on a reorganizing debtor. In fact, a reorganization plan which does not deal with rates could well be a lawful plan. However, for an enterprise such as PSNH, the success of the enterprise and the funding of the plan are dependent upon the rates the Debtor may charge. In section 1129(a)(6), Congress made the determination that the rare utility debtor which finds itself in Chapter 11 proceedings must solve the problem of disparity between its revenues and its expenditures that will in all likelihood have been the reason for its Chapter 11 filing. Congress has mandated that for a public utility debtor to emerge from reorganization, with a plan funded by a rate change, the rate change must be "approved"; it cannot be merely proposed, it cannot be under consideration, and it cannot be in effect under bond subject to refund. The rate change must be first approved so that the court and the constituencies dealing with the reorganized entity can be reasonably assured that the reorganized utility will not completely self-destruct upon the resolution of the outstanding rate issue. Plan feasibility is the function of section 1129(a)(6), and the progress of this proceeding demonstrates the wisdom of Congress in requiring it.

Section 1141 of the Bankruptcy Code addresses the effect of confirmation. In section 1141(a) the entities bound by a confirmed plan are identified. Regulatory authorities are not

included in the section. Ignoring the import of section 1141 is one of the major flaws in the analysis of PSNH and the Committees. They describe the provisions of section 1123(a) as "self-executing", but fail recognize that it is section 1141 that makes plan provisions self-executing. Section 1141 does not make the provisions of confirmed plans "self-executing" to the extent that they affect the public's right to the protections provided by state and federal police power laws.

This critical distinction renders inapplicable the analysis of the United States Court of Appeals for the Fourth Circuit in the case of In re FCX, Inc. 853 F.2d 1149 (4th Cir. 1988). That case involved a right akin to call protection asserted by a secured creditor to block the distribution of collateral to the creditor in satisfaction of its secured claim. Although the FCX case does not discuss section 1141, it is the fact that a confirmed plan binds creditors under section 1141 that created the preemptive effect found by the Fourth Circuit. The rights of governments to enforce valid police power laws and the rights of the public to the protections that such laws provide were not implicated in FCX.

Section 1142 relates to the implementation of the plan. Truly, if Congress were to take the approach urged by the Debtor and the Committees, one would find clear language to that effect in section 1142 relating to the implementation of plans. The

original bankruptcy reform legislation would have so provided, see infra page 53-56, but that language was not enacted.

"Notwithstanding" language is found in section 1142, but it is very narrow. Section 1142(a) provides that:

Notwithstanding any otherwise applicable non-bankruptcy law, rule, or regulation relating to financial condition, the debtor and any entity organized or to be organized for the purpose of carrying out the plan shall carry out the plan and comply with any order of the court.

11 U.S.C. §1142(a) (emphasis added).

The "notwithstanding" language in section 1142(a) is confined to specific types of non-bankruptcy laws. It constitutes the limited reach of the Bankruptcy Code into non-bankruptcy law, beyond laws pertaining to the rights of holders of claims and interests, in the implementation of reorganization plans.

As previously noted, the construction of the bankruptcy code is a "holistic" endeavor. United Savings Assoc. of Texas v. Timbers of Inwood Forest Assocs., 484 U.S. 365, ___ 98 L.Ed.2d 740, 748 (1988). PSNH and the Committees have taken a phrase at the beginning of section 1123(a) of the Bankruptcy Code, which was added as a "non-substantive" amendment in 1984, and attempted with it to fashion powers for reorganizing entities that go far beyond any of those intended by Congress. Review of the overall statutory framework makes clear that the type of express pronouncement from Congress that one would expect in connection

with such a major displacement of federal and state police powers is simply absent.

At least two other features of the language of the Bankruptcy Code make the PSNH interpretation of section 1123(a) implausible. First, where Congress did actually provide for provisions relating to implementation of plans, namely, in section 1142, Congress provided for carrying out the plan "notwithstanding any otherwise applicable non-bankruptcy law, rule or regulation relating to financial condition...." 11 U.S.C. §1142(a) (emphasis added). This language would have been unnecessary surplusage if Congress had intended the sweep of the "notwithstanding" language of 1123 to be as broad as suggested by PSNH.

Similarly, section 363(1) of the Bankruptcy Code, as it relates to Chapter 11 plans, would be unnecessary if section 1123(a) were interpreted as PSNH suggests. Section 363(1) provides that:

(1) Subject to the provisions of section 365, the trustee may use, sell, or lease property under subsection (b) or (c) of this section, or a plan under chapter 11, 12, or 13 of this title may provide for the use, sale, or lease of property, notwithstanding any provision in a contract, a lease, or applicable law that is conditioned on the insolvency or financial condition of the debtor, on the commencement of a case under this title concerning the debtor, or on the appointment of or the taking possession by a trustee in a case under this title or a custodian, and that effects, or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in such property.

11 U.S.C. §363(1) (emphasis added).

Indeed, if PSNH construction of section 1123(a) is accepted, the provisions of sections 1141(a) and 1142(a) in their entirety could well be unnecessary. However, these provisions in sections 1141, 1142 and 363 cannot be construed as surplusage; they represent the limited and precise preemptive actions of Congress relating to the implementation of reorganization plans. Sutherland, Statutes and Statutory Construction §46.05 (4th ed. 1986) ("A statute is passed as a whole and not in parts or sections and is animated by one general purpose and intent. Consequently, each part or section should be construed in connection with every other part or section so as to produce a harmonious whole. Thus it is not proper to confine interpretation to the one section to be construed.").

Section 1123 spells out Congress' intention that federal law should cover what are to be the mandatory and permissive terms of reorganization plans. Section 1141 sets forth the effect of a confirmed plan on the rights of creditors and equity security holders. Sections 1142 and 363(1) spell out Congress' intent to preempt in relation to plan implementation. The reference in the legislative history to this effect cited in the Creditors' Committee memorandum (page 7 n.1) is no "error" as suggested by the Committee. The fit of the statutory language and the expression of legislative history make perfect sense if the appropriate construction is applied to section 1123(a).

II. THE CANONS OF STATUTORY CONSTRUCTION COMPEL THE CONCLUSION THAT CONGRESS DID NOT INTEND TO PREEMPT STATE POLICE POWER REGULATION OF MONOPOLY UTILITIES.

In addition to dealing with the statutory language itself, the United States Supreme Court has on many occasions addressed the question of whether Congress intended to preempt state law with particular enactments. In this section of the State's memorandum, the State will first demonstrate that the United States Supreme Court has rejected the argument that the language of the type contained in 28 U.S.C. §1334 relating to jurisdiction over debtors indicates preemptive intent. The State will then show that the tests outlined by the United States Supreme Court for finding preemption clearly demonstrate that no preemptive intent of Congress can be found here.

- A. The United States Supreme Court has rejected the argument that a grant of exclusive jurisdiction over property of a debtor preempts state law.

One argument which PSNH makes in support of its argument that the Bankruptcy Code preempts state police power laws pertaining to the regulation of public utilities is based on the grant of jurisdiction conferred upon the district courts under 28 U.S.C. §1334(d), which provides that:

(d) The district courts in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction of all of the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate.

28 U.S.C. §1334(d). PSNH asserts in its "Motion for Summary Judgment":

Section 1123(a)(5) of the Bankruptcy Code, coupled with the grant of plenary jurisdiction of the property of the debtor and the property of the estate under 28 U.S.C. §1334(e) [sic], vests power in this Court to confirm and implement a chapter 11 plan (and specifically the plan filed by Public Service on December 27, 1988) without compliance with otherwise applicable non-bankruptcy law restricting or conditioning the transactions contemplated under such a chapter 11 plan.

Court Paper No. 1634, at 2.

The issues arising under section 1123 are discussed at length elsewhere in this memorandum. However, a brief discussion of the argument regarding the jurisdiction of the district court under section 28 U.S.C. §1334(d) is in order.

First, it should be noted that although PSNH relies on 28 U.S.C. §1334(d) in its Motion for Summary Judgment, PSNH's fifty-six page memorandum supporting its motion fails to mention the section, and with good reason. The language of 28 U.S.C. §1334(d) is substantially the same as the language which was contained in section 77(a), which provided the Bankruptcy Court with "exclusive jurisdiction of the debtor and its property wherever located...." Bankruptcy Act of 1898, §77(a).

In Palmer v. Massachusetts, 308 U.S. 79, 84 L.Ed. 93 (1939) the United States Supreme Court, in a unanimous opinion written by Justice Frankfurter, rejected arguments that this language together with the provisions of section 77(c)(2), which permits

trustees subject to the court's control to operate the business of the debtor, formed the basis for preemption of local regulatory laws pertaining to intrastate railroad lines. The court stressed the historic importance of local control over railroads and stated that "... if this old and familiar power of the state was withdrawn when Congress gave district courts bankruptcy powers over railroads, we ought to find language fitting for so drastic a change." *Id.* at 85. The court rejected the argument that the jurisdictional provisions of section 77(a) provided the requisite language.

This decision is directly on point with respect to PSNH's argument concerning the effect of 28 U.S.C. §1334(d). Therefore, this argument must be summarily rejected.

- B. The tests for preemption established by the United States Supreme Court do not support the proposition that Congress preempted public utility laws.

The line of cases articulated by the United States Supreme Court in relation to preemption clearly show that the requisite intent of Congress to preempt utility regulation in section 1123(a) of the Bankruptcy Code, either in 1978 or 1984, is not present, particularly with respect to an area of such substantial state concern as the regulation of public utilities. The Court must be mindful that the enterprise with which we are dealing here is a public utility, a privately owned monopoly engaged in

the business of providing essential services to the public. Thus, when looking at a determination of whether Congress has chosen to "occupy the field", it is critical to define just what the "field" is. Here, it is the regulation of public utilities. Furthermore, the proposition urged on this Court involves the question of whether Congress intended to supplant a state regulatory system with no corresponding regulatory framework. Viewed from this perspective, it is clear that the requisite Congressional intent to preempt cannot be found.

The question of whether a particular federal act preempts state laws is a question of congressional intent. Jones v. Rath Packing Co., 430 U.S. 519, 51 L.Ed.2d 604 (1977). Statutory construction plays a large role in determining congressional intent.

PSNH and the Committees claim that no statutory construction is necessary; the isolated five words at the beginning of section 1123(a) of the Bankruptcy Code are the plain language of Congress which ends all further inquiry. In this regard, the memorandum of the Creditors' Committee incorrectly emphasizes on United States v. Ron Pair Enters., Inc., ___ U.S. ___, 103 L.Ed.2d. 290 (1989), in which the Court stated:

The task of resolving the dispute over the meaning of section 506(b) begins where all inquiries must be begin: with the language itself....In this case it is also where the inquiry should end, for where, as here, the statute's language is plain, "the sole function of the courts is to enforce it in accordance to its terms.

Id. at 298 (citation omitted).

The Court in Ron Pair was dealing with a question of whether section 506(b) provided for the allowance of post-petition interest to oversecured holders of non-consensual liens. The Court relied on two key factors in its determination to deal with the statutory language and no more. First, the Court concluded that the language was plain and that it did not produce "a result demonstrably at odds with the intention of its drafters." Id. at 299. (citing Griffin v. Oceanic Contractors, Inc., 458 U.S. 564 (1982)). Second, the Court concluded that the plain meaning of the contested provision did "not conflict with any other section of the Code, or with any important state or federal interests; nor [was] a contrary view suggested by the legislative history." Id. The Court distinguished Kelly v. Robinson, 479 U.S. 36, 93 L.Ed.2d 216 (1986), and Midlantic National Bank v. New Jersey Department of Environmental Protection, 474 U.S. 494, 88 L.Ed.2d 859 (1986), which are discussed below, on the grounds that those two cases

...concerned statutory language which, at least to some degree, was open to interpretation. Each involved a situation where bankruptcy law, under the proposed interpretation, was in clear conflict with state or federal laws of great importance. In the present case, in contrast, the language in question is clearer than the language at issue in Midlantic and Kelly: as written it directs that the post-petition interest be paid on all oversecured claims. In addition, this natural interpretation of the statutory language does not conflict with any significant state or federal interest, nor with any other aspect of the Code.

Id. at 301.

In this case, we are not addressing statutory language of the type examined by the Court in Ron Pair. First, some level of interpretation must be applied to the introductory phrase of section 1123(a). The Debtor and the Committees cannot seriously be suggesting that, in order to maximize value for the purpose of reorganizing a debtor, every law outside of the Bankruptcy Code, state or federal, civil or criminal, can be brushed aside by the reorganizing debtor. However, that is the result of their expansive view of section 1123(a); that the sweep of its language extends not only to the content of plans, but to the implementation of plans. Such a grant of power, tempered by nothing other than the needs of the constituents benefited by the plan, cannot be inferred. Furthermore, this interpretation does not square with the language that Congress did provide in sections such as 1142 and 363(1). It also would be in clear conflict with state or federal laws of great importance. Arkansas Elec. Coop. v. Arkansas Pub. Serv. Comm'n, 461 U.S. 375, 377, 76 L.Ed.2d 1, 6 (1983) ("[T]he regulation of utilities is one of the most important of the functions traditionally associated with the police power of the States.").

The five words at the beginning of section 1123(a) of the Bankruptcy Code are not the type of plain, unambiguous language that obviate the need to apply the canons of statutory

construction. Application of those canons compels the conclusion that Congress did not intend to preempt fundamental state interests.

The general rule of construction is that "the historic police powers of the States [are] not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress." Jones v. Rath Packing Co., 430 U.S. 519, 525, 51 L.Ed.2d 604, 614 (quoting Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947)). The process was described by Justice Frankfurter in Palmer v. Massachusetts as follows:

Plainly enough the District Court had no power to deal with a matter in the keeping of state authorities unless Congress gave it. And so we have one of those problems in the reading of a statute wherein meaning is sought to be derived not from specific language but by fashioning a mosaic of significance out of the innuendos of disjointed bits of a statute. At best this is subtle business, calling for great wariness lest what professes to be mere rendering becomes creation and attempted interpretation of legislation becomes legislation itself. Especially is wariness enjoined when the problem of construction implicates one of the recurring phases of our federalism and involves striking a balance between national and state authority in one of the most sensitive areas of government.

[I]n construing legislation this court has disfavored inroads by implication on state authority and resolutely confined restrictions upon the traditional power of states to regulate their local transportation to the plain mandate of Congress.

Palmer, 308 U.S. at 83-84.

The task in resolving this issue, therefore, depends on finding the "manifest intention" or "plain mandate" of Congress to deregulate utilities with respect to all transactions contemplated in reorganization plans other than rate changes. Furthermore, we must do so in an environment where no replacement regulatory mechanism is prescribed. As in the case of Puerto Rico Consumer Affairs Department v. Isla Petroleum Corp., 485 U.S. 495, 99 L.Ed.2d 582 (1988):

...we are presented with the decidedly untypical claim that federal pre-emption exists despite, not only the absence of a statutory provision specifically announcing it, but the absence of any extant federal regulatory program with which the state regulation might conflict and which might therefore be thought to imply pre-emption.

We have suggested elsewhere that the Constitution permits Congressional creation of such a regime. See, e.g., Arkansas Electric Cooperative Corp. v. Arkansas Public Service Comm'n., 461 U.S. 384, 76 L.Ed.2d 1, 103 S Ct 1905 (1983). But to say that it can be created is not to say that it can be created subtly.

Id. at 589.

There is no express provision in Title 11 for federal regulation of public utilities. Although the bankruptcy court, as a court in equity, must deal with the public interest in entering equity-orders, and public interest principles can be construed to be part of the inherent powers of the Bankruptcy Code under section 105 of the Bankruptcy Code and perhaps part of the determination of whether a plan is proposed in good faith

under section 1129(a)(3), there is no express provision for the replacement of the State regulatory process PSNH and the Committees propose to displace. There is no federal structure for determining which transactions will be subjected to public interest review, nor is there a statutory or regulatory framework providing the court with guidance as to how the public interest is to be protected.

Instituting a standardless grant to the judiciary of authority to regulate utilities rather than providing a legislative grant to an administrative agency is wholly inconsistent with the history of federal and state legislation since at least the turn of the century. Even in the case of reorganizing railroads, where the public interest role of the Bankruptcy Court under both the Act and the Code have been explicit, there is a structure providing for an administrative agency to be actively involved throughout the case. There is no such structure for public utility debtors. In short, Congress has provided no federal regulatory scheme to fill the void which would be created by the preemption of state regulatory authority for reorganizing debtors.

Another potential ground for finding preemptive intent on the part of Congress is that the State statute or regulatory activity actually conflicts with federal law. For example, in Mississippi Power & Light Co. v. Mississippi, ___ U.S. ___, 101 L.Ed.2d 322

(1988), the United States Supreme Court held that in a multi-state holding company power pool context, a determination by the FERC to allocate generating resources to particular affiliated retail companies preempted states from attempting to redo the allocations through separate prudency reviews. In that case, the utilities involved would be unable to comply with both the federal and state regulatory determinations in the event those determinations disagreed.

The Supreme Court, however, has exercised great care in finding conflicts. In Exxon Corp. v. Governor of Maryland, 437 U.S. 117, 57 L.Ed.2d 91 (1978), the Court upheld a Maryland statute relating to the regulation of gasoline retailers in the face of a challenge that the statute violated federal antitrust laws. The Court cautioned that:

[i]n this as in other areas of coincident federal and state regulation, the 'teaching of this court's decisions...enjoin[s] seeking out conflicts between state and federal regulation where none clearly exists.'

Id. at 130 (citations omitted).

Similarly, state power plant siting regulations relating to economic considerations in whether to construct nuclear power plants were held not to conflict with health and safety regulation of nuclear power plant construction by the Nuclear Regulatory Commission in Pacific Gas and Electric Company v. State Energy Resources Conservation and Development Commission. 461 U.S. 190, 75 L.Ed.2d 752 (1983).

There has been no demonstration in this case that a plan which complies with New Hampshire law cannot be devised. New Hampshire has procedures for the approval of transactions such as the transfer of assets, the granting of franchises, and the issuance of securities that are fair and reasonable. Furthermore, in the face of important utility interests, the NHPUC has a history of taking the steps necessary to adjudicate petitions expeditiously while protecting the rights of all participants. Indeed, the record of the NHPUC in handling complex matters pertaining to PSNH certainly compares very favorably with the one-year time schedule outlined by PSNH for its proposed FERC proceeding.

This is not a case of incompatibility of state law and federal law. This is a case in which the Debtor and the Committees have concluded, plainly and simply, that the distributions to them will be increased in the event that state law is preempted. However, profit to private constituencies has been rejected by the United States Supreme Court as a basis for finding preemption. In Louisiana Public Service Commission v. Federal Communication Commission, 476 U.S. 355, 90 L.Ed.2d 369 (1986), the Court addressed the issue as follows:

[w]hat is really troubling respondents, of course, is their sense that state regulators will not allow them sufficient revenues. While we do not deprecate this concern, [the jurisdictional separation provision] precludes both the FCC and this Court from providing the relief sought.

476 U.S. at 376.

Finally, the ability of state utility regulation and federal bankruptcy law to co-exist is demonstrated by the fact that no one disputes that the bankruptcy laws and state utility regulations did, in fact, co-exist under the Bankruptcy Act.

In looking at whether state regulatory laws either conflict or interfere with the Bankruptcy Code, it can readily be seen that the efforts of state regulators on the one hand and the reorganization court on the other are directed at different objectives and statutory standards. For example, in looking at the section 1129 provisions relating to the standards for confirmation, the NHPUC will not be examining whether the plan or its proponent have complied with the provisions of Title 11 (11 U.S.C. §1129(a)(1) & (2)), that the plan has been proposed in good faith (11 U.S.C. §1129(a)(3)), that payments to professionals have been approved by the court (11 U.S.C. §1129(a)(4)), or that the treatment of impaired or unimpaired claims or interests conform to Code provisions (11 U.S.C. §1123(a)(7)-(10); 11 U.S.C. §1129(b)).

The scope of NHPUC review is whether the various proposed transactions over which it has statutory jurisdiction are consistent with the public good. Only through this examination can the basic rate formula which it will subsequently use function in the manner intended. If asset transfers are

contemplated utilizing prices that reflect "write-ups" which cannot be squared with the public good, if securities are issued in such amounts that they vastly exceed the value of rate base assets for ratemaking purposes, if cash flows depend on depreciation and other accounting techniques that are inconsistent with state regulations, if contracts between the resulting utility companies and affiliates provide for costs that are excessive and disproportionate to services which the reorganized utilities could obtain elsewhere for less, the NH PUC's ratemaking tool, which provides a rate of return (cost of capital) on rate base (level of investment) after expenses (prudently incurred) simply will not work. As a result, the construction of the Bankruptcy Code proposed by PSNH and the Committee results not only in preemption of all regulatory activity except with respect to rate changes, but in the substantial impairment of regulation of rate changes. See State v. Kansas City Gas Co., 163 S.W. 854, 858 (1913) ("every expenditure, every dereliction, every share of stock, or bond, or note issued as a surety is finally reflected in rates and quality of service to the public....").

The case of Perez v. Campbell, 402 U.S. 637, 29 L.Ed.2d 233 (1971), is cited by the Creditors' Committee as support for the proposition that Congress intended to preempt utility regulation in connection with implementation of reorganization plans. That

case, however, involved a deliberate and unabashed effort to undercut the effect of a bankruptcy discharge. Under an Arizona statute, unpaid tort judgments arising out of automobile accidents could result in the inability of the judgment debtor to obtain a driver's license in the State of Arizona. Furthermore, the statute contained what the court characterized as an "anti-discharge" section expressly providing that "[a] discharge in bankruptcy following the rendering of any such judgment shall not relieve the judgment debtor from any of the requirements of this article." Perez, 402 U.S. at 642 (citing Ariz. Rev. Stat. Ann. §28-1163(B)).

The Supreme Court characterized the Arizona statute as "one with a declared purpose to protect judgment creditors 'from financial hardship' by giving them a powerful weapon with which to force bankrupts to pay their debts despite their discharge." Id. at 654. The Court held that the Arizona statute had both the purpose and effect of frustrating federal law. Id.

There is no such purpose or effect here. What the State is attempting to accomplish in this proceeding is to provide for the enforcement of neutral state laws affecting public utilities. In this sense, the case is akin to the cases of Kelly v. Robinson, 479 U.S. 36, 93 L.Ed.2d 216 (1986), and Midlantic National Bank v. New Jersey Department of Environmental Protection, 474 U.S. 494, 88 L.Ed.2d 859 (1986).

In Kelly, the United States Supreme Court addressed the question of whether restitution obligations, imposed as conditions of probation in state criminal proceedings, are dischargeable in Chapter 7 cases. The Court, guided by "the fundamental policy against federal interference with state criminal prosecutions"⁴ held that such obligations were excepted from discharges by section 523(a)(7), which excludes from discharges any debt "to the extent such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss." Kelly, 474 U.S. at 41 (citing 11 U.S.C. §523(a)(7)).

In reaching its decision, the Court declined to read the Bankruptcy Code in a vacuum.

Of course, the 'starting point in every case involving construction of a statute is the language itself.' [Citation omitted] But the text is only the starting point.... ' In expounding a statute, we must not be guided by a single sentence or a member of a sentence, but look to the provisions of the whole law, and to its object and policy.'" [Citation omitted] In this case, we must consider the language of §§101 and 523 in light of the history of bankruptcy court deference to criminal judgments and in light of the interests of the States in unfettered administration of their criminal justice systems.

Id. at 43-44.

'[W]e do not read these statutory words with the ease of a computer. There is an overriding consideration that

4/ Kelly, 479 U.S. at 47 (citing Younger v. Harris, 401 U.S. 37 (1971)).

equitable principles govern the exercise of bankruptcy jurisdiction.' [Citation omitted] This court has recognized that States' interest in administering their criminal justice systems free from federal interference is one of the most powerful considerations that should influence a court considering equitable types of relief. [Citing Younger.] This reflection of our federalism also must influence our interpretation of the Bankruptcy Code in this case.

Id. at 49.

At this point, the Court went on in footnote 11 to state:

Justice Frankfurter advocated a similar approach to the interpretation of regulatory statutes that infringe upon important state interests. 'The task is one of accommodation as between assertions of new federal authority and historic functions of the individual states. Federal legislation of this character cannot therefore be constructed without regard to the implications of our dual system of government....The underlying assumptions of our dual form of government, and the consequent presuppositions of legislative draftsmanship which are expressive of our history and habits, cut across what might otherwise be the implied range of legislation. The history of congressional legislation...justif[ies] the generalization that, when the Federal Government takes over such local radiations in the vast network of our national economic enterprise and thereby radically readjusts the balance of state and national authority, those charged with the duty of legislating are reasonably explicit.'

Id. at 49 n.11 (quoting, Frankfurter, Some Reflections on the Reading of Statutes, 47 Colum. L. Rev. 527, 535-40 (1947)).

The parallels between the state interests in its criminal justice system and in its exercise of regulatory authority over public utilities are obvious. Just as the Younger line of cases have developed abstention principles in relation to interference with state court proceedings, so too has such a line of cases

developed with respect to state regulatory proceedings. See, e.g., Alabama Pub. Serv. Comm'n v. Southern Ry. Co., 341 U.S. 341, 95 L.Ed. 1002 (1951); Burford v. Sun Oil Co., 319 U.S. 315, 87 L.Ed. 1424 (1943).

With respect to state criminal laws, the Court in Kelly stated:

[i]f Congress had intended, by section 523(a)(7) or by any other provision, to discharge state criminal sentences, 'we can be certain that there would have been hearings, testimony and debate concerning consequences so wasteful, so inimical to purposes previously deemed important, and so likely to arouse public outrage.'

Id. at 51 (citation omitted).

Similarly, this adversary proceeding involves state interests which the Court in Arkansas Electric Cooperative characterized as "...one of the most important of the functions traditionally associated with the police power of the states." Arkansas Elec. Coop., 461 U.S. at 377. Nevertheless, the Debtor and its Committees make their proposal despite the complete absence of any hearings, testimony, debates, or even comments on the pre-emption issue during the legislative process of the Bankruptcy Reform Act of 1978. It is inconceivable that this extraordinary and radical departure from pre-Code practice involving such important state interests would not warrant any mention whatsoever in the legislative history given the

deliberate and exacting process of Congress in its reform of the Bankruptcy Act.

Congress heard extensive testimony and conducted numerous hearings during the eight year evolution of the Bankruptcy Code. Hearings on only two of the early versions of the Bankruptcy Reform Act, H.R. 31, 94th Cong., 1st Sess. (1975) and H.R. 32, 94th Cong., 1st Sess. (1975), consumed at least thirty-five days. Thousands of pages of Hearing Reports on these proposals alone were published. A thorough review of the Hearing Reports, debates, and testimony published during this eight year legislative process reveals one glaring omission. Over the eight year legislative period Congress never debated whether section 1123 would preempt all otherwise applicable regulatory laws governing public utilities. According to the Debtor and its Committees, Congress plainly preempted such laws. Yet this supposedly plain, but clearly radical and extraordinary departure from pre-Code practice was not the subject of even one comment or objection during the legislative process. Such a possibility is inconceivable.

As already noted, the United States Supreme Court has made clear that congressional silence may be of extreme significance when determining congressional intent. Kelly v. Robinson, 479 U.S. 36, 50-51, 93 L.Ed. 2d. 216, 229-30

(1986) ("[i]f Congress had intended, by section 523(a)(7) or by any other provision, to discharge state criminal sentences, 'we can be certain that there would have been hearings, testimony and debate concerning consequences so wasteful, so inimical to purposes previously deemed important, and so likely to arouse public outrage....'");

Midlantic Nat'l Bank v. New Jersey Dept. of Env'tl. Protection, 474 U.S. 494, 501, 88 L.Ed.2d. 859, 866

(1986) (if Congress had wished to grant the trustee an extraordinary exemption from non-bankruptcy law, "the intention would [have been] clearly expressed, not left to be collected or inferred from disputable

considerations...."); Mastro Plastics v. National Labor Relations Board, 350 U.S. 270, 289, 100 L.Ed. 309, 323

(1956) ("Congress cannot fairly be held to have made such an intrusion on employees' rights...without some more explicit expression of its purpose...."). See also National Assoc. for the Advancement of Colored People v. Civiletti, 609 F.2d 514, 519 (D.C. Cir. 1979) ("Had Congress intended to abrogate federal sovereign immunity for purposes of the Awards Act, some discussion of the matter by the respective House and Senate Committees responsible for the legislation in their Committee Reports might have been expected."); Sutherland,

Statutes and Statutory Construction §48.06 (4th ed. 1986).

The Debtor and its Committees ignore the obvious.

Preemption is only found when it is the clear and manifest purpose of Congress." Jones v. Rath Packing Co., 430 U.S. 519, 525, 51 L.Ed.2d 604, 614 (1977) (quoting Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230 (1947)). It is not lightly presumed by a court. See Florida Lime and Avocado Growers v. Paul, 373 U.S. 132, 10 L.Ed.2d 248, 257 (1963) (federal regulation of commerce does not preempt state regulatory power absent "persuasive reasons"). The idea that Congress preempted an entire body of both state and federal regulatory laws without so much as one debate, one hearing, one instance of testimony on why such a radical change was necessary to the reform initiative is not only preposterous, but contrary to the legislative process Congress undertook in formulating the present bankruptcy laws.

Congress' silence in this case speaks volumes. If Congress had intended section 1123 to preempt state and federal laws regulating public utilities, then it would have addressed, if even in one brief passage, why it had elected to preempt state and federal regulatory control over public utilities in the formation, confirmation, and implementation

stages of a reorganization plan during a Chapter 11 proceeding.

Similarly, in Midlantic, the Supreme Court held that the abandonment power of bankruptcy trustees does not authorize such trustees to abandon hazardous waste sites in contravention of state laws or regulations that are reasonably designed to protect the public's health or safety. The Court stated:

[if] Congress wishes to grant the trustee an extraordinary exemption from non-bankruptcy law 'the intention would be clearly expressed, not left to be collected or inferred from disputable considerations of convenience in administering the estate of the bankruptcy.' [Citation omitted] See Palmer v. Massachusetts, 308 U.S. 79 ("If this old and familiar power of the states [over local railroad service] was withdrawn when Congress gave district courts bankruptcy powers over railroads, we ought to find language fitting for so drastic a change.") Although these cases do not define for us the exact contours of the trustee's abandonment power, they do make clear that this power was subject to certain restrictions when Congress enacted Section 554(a).

Midlantic, 474 U.S. at 501.

The Court also drew by analogy on the provisions of 28 U.S.C. §959(b).³ The Court stated as follows:

2/ 28 U.S.C. §959(b) provides:

Except as provided in section 1166 of title 11, a trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the

(Footnote 3 continued on next page)

Title 28 U.S.C. §959(b) provides additional evidence that Congress did not intend for the Bankruptcy Code to pre-empt all state laws. Section §59(b) commands the trustee to 'manage and operate the property in his possession...according to the requirements of valid laws of the State.' The petitioners have contended that §959(b) is relevant only when the trustee is actually operating the business of the debtor, and not when he is liquidating it. Even though §959(b) does not directly apply to an abandonment under §554(a) of the Bankruptcy Code - and therefore does not delimit the precise conditions on an abandonment - the section nevertheless supports our conclusion that Congress did not intend for the Bankruptcy Code to pre-empt all state laws that otherwise constrain the exercise of a trustee's powers.

Id. at 505.

Although 28 U.S.C. §959(b) does not directly pertain to the implementation of plans of reorganization, it reinforces the conclusion that the general policy of Congress is not to permit reorganizing debtors to transgress state police power laws, and expressions of contrary congressional intent must necessarily be more explicit than any of those articulated by PSNH and the Committees.

- C. The development of the Bankruptcy Code reflects the affirmative intent of Congress to leave intact state regulatory requirements.

(Footnote 5 continued from previous page)
owner or possessor thereof would be bound to do if in possession thereof.

At the time of the adoption of the Bankruptcy Code in 1978, Congress had before it three distinct models for dealing with state police power laws relating to regulated entities.

The railroad reorganization model was reflected in section 77 of the Bankruptcy Act. The section 77 process provided for the consideration of all reorganization plans by the Interstate Commerce Commission ("ICC"). See Bankruptcy Act of 1898, §77(d). No reorganization plan could be approved by the ICC unless the ICC found that the plan would "... be compatible with the public interest." Furthermore, section 77(d) provided that "[n]o plan shall be approved or confirmed by the judge in any proceeding under this section unless the plan shall first have been approved by the Commission and certified to the court." With this full public interest review constituting a precondition to the confirmation of any plan, Congress then took the preemptive step of providing in the plan implementation provisions of section 77(f) that the reorganized entity would have authority to carry out the plan, "the laws of any State or the decision or order of any State authority to the contrary notwithstanding."⁶ Thus, under the section 77 model, there was full participation by a regulatory authority, the ICC, in the reorganization process, and

^{6/} The express provisions of §77(f) explain the language in railroad reorganization cases relating to the preemptive effects of railroad reorganization plans. See, e.g., Calloway v. Benton, 336 U.S. 132, 93 L.Ed. 553 (1949), Palmer v. Massachusetts, 308 U.S. 79, 84 L.Ed. 93 (1939).

a full public interest veto over any plan of reorganization. Section 77, which implements national policy relating to the availability of rail transportation as well as the reorganization of debtors, provided for preemption in plain language with an express statutory procedure for protection of the public interest.

At the other end of the spectrum were the provisions relating to the reorganization of public utilities under Chapter X of the Bankruptcy Act. In Chapter X proceedings, there was no regulatory authority such as the ICC sitting at the right hand of the bankruptcy judge. Instead, full compliance with the requirements of regulatory authorities was mandated for the entities resulting from the reorganization. In addition, state regulatory authorities were given powers as a matter of federal law in the reorganization process. Section 224 of the Bankruptcy Act provided:

Upon confirmation of a plan -

(2) the debtor and every other corporation organized or to be organized for the purpose of carrying out the plan shall comply with the provisions of the plan and with all orders of the court relative thereto and shall take all action necessary to carry out the plan, including, in the case of a public-utility corporation, the procuring of authorization, approval, or consent of each commission having regulatory jurisdiction over the debtor or such other corporation.

Thus, Congress had provided for full compliance with state police power laws pertaining to regulated industries, including provisions for the protection of the public interest.

Moreover, Congress provided state regulatory authorities with powers to protect the public interest that went beyond state law provisions. Sections 177 and 178 of the Bankruptcy Act provided:

177. In case a debtor is a public-utility corporation, subject to the jurisdiction of a commission having regulatory jurisdiction over the debtor, a plan shall not be approved, as provided in section 174 of this Act, until -

(1) It shall have been submitted to each such commission;

(2) An opportunity shall have been afforded each such commission to suggest amendments or offer objections to the plan; and

(3) The judge shall have considered such amendments or objections at a hearing at which such commission may be heard.

178. In case a debtor is a public utility corporation, wholly intrastate, subject to the jurisdiction of a State commission having regulatory jurisdiction over such debtor, a plan shall not be approved, as provided in section 174 of this Act, unless such State commission shall have first certified its approval of such plan as to the public interest therein and the fairness thereof. Upon its failure to certify its approval or disapproval within 30 days, or such further time as the court may prescribe, after the submission of the plan to it, as provided in section 177 of this Act, the public interest shall, for the purpose of such approval and of the confirmation of the plan, not be deemed to be affected by the plan.

In these two sections Congress provided state regulatory authorities with authorizations that went beyond the ability to

approve specific transactions under state regulatory statutes. In section 177, the regulatory commissions were given authority to comment on and to suggest amendments to entire plans of reorganization. The regulatory commissions were not confined to objections based on state law issues or specific state regulatory requirements. Presumably then, regulatory commissions could make comments relating to distribution provisions of plans as well as provisions relating to the structure of the non-regulated portion of the reorganized entities.

In the case of intrastate public utilities, the grants of power to state regulatory authorities under federal law were even broader. State commissions were granted approval power with respect to the impact of the plan on the public interest and as to the "fairness" of the plan. In these provisions, Congress went beyond recognizing and leaving in place the police powers of states. It took the additional step of providing state regulatory authorities with the power under federal law to participate in the plan process and, in the case of an intrastate utility, actually to approve or disapprove plans.

The third model was Chapter XI of the Bankruptcy Act which was completely silent with respect to state regulatory laws. There was no provision comparable to section 224(2) mandating regulatory approvals. At the same time, there were no provisions relating to the contents of plans of arrangement comparable to

the section 1123(a) provisions of the Bankruptcy Code relied upon by the Debtor and the Committees.

In enacting the Bankruptcy Code, Congress was faced with a number of alternatives with respect to the treatment to be accorded to state regulatory laws and the mechanism to be devised for protection of the public interest in reorganization cases. The choices can be summarized as follows:

1. Taking the approach suggested by PSNH and the Committees of preempting all state police power laws and ignoring the public interest.

2. Taking the approach of Section 77 by having plan confirmation subject to a precondition that a specified regulatory commission involved in the case determine that the plan is consistent with the public interest and, after that determination, preempting state laws.

3. Taking the approach of Chapter X by mandating compliance with state law and providing state regulatory agencies with powers under federal law to affect the reorganization process.

4. Taking the approach of Chapter XI by leaving state laws intact and having the public interest in transactions contemplated by plans adjudicated in the appropriate regulatory forums.

The legislative history and the structure of Chapter 11 of the Bankruptcy Code show that in the case of entities other than

railroads, Congress adopted the approach of Chapter XI of the Act, namely, having no specifically prescribed regulatory approval process within the Chapter 11 proceeding and leaving in place the state regulatory processes. In the case of railroads, Congress adopted a modified process in which both ICC involvement in the reorganization process was prescribed and state laws were left fully in effect except in certain specified instances. See 11 U.S.C. §1166. Furthermore, in railroad reorganizations, Congress expressly provided for protection of the public interest. 11 U.S.C. §1165 ("In applying sections 1166, 1167, 1169, 1170, 1171, 1172, 1173 and 1174 of this title, the court and the trustee shall consider the public interest in addition to the interests of the debtor, creditors, and equity security holders."). These latter provisions can hardly be characterized to reflect a congressional mood of abandonment of the public interests in reorganization cases.

With respect to public utilities in Chapter 11 cases, Congress considered and rejected a statutory framework in which reorganization plan provisions would preempt state regulatory laws. In 1970 Congress established the Commission on the Bankruptcy Laws of the United States. The Commission was established in response to growing criticism of the Act. The purpose of the Commission was to study, analyze, evaluate and

recommend substantive changes to the Act. 2 Collier on Bankruptcy (Appendix) VII (15th Ed. 1988).

The Commission released its report and recommendations in 1973. Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc. No. 137, 93rd Cong., 1st. Sess. 23 (1973) (hereinafter the "Commission Report"). The Commission Report included a draft of a new bankruptcy act. This bill was introduced in both Houses in 1973, on the Senate side as S. 2565, 93d Cong., 1st Sess. (1973), and on the House side as H.R. 10792, 93d Cong., 1st Sess. (1973). Congress did not act on this proposed legislation, but in 1974 the Commission bill was reintroduced as H.R. 31, 94th Cong., 1st Sess. (1975) and S. 236, 94th Cong. 1st Sess. (1974). Although some of the language pertinent to regulation in these bills and in a competing proposal put forth by the National Conference of Bankruptcy Judges, was adopted,⁷ it is important to examine what Congress choose not to adopt. The implementation provisions, which

Z/ See S. 235, 94th Cong., 1st Sess. (1974); H.R. 32, 94th Cong., 1st Sess. (1975) which provided:
(d) Confirmation. The court shall confirm a plan if

(F) Any regulatory commission having jurisdiction over the debtor has approved any rate change provided for in the plan, or such rate change is expressly made subject to the obtaining of such approval.

See, also, Commission Report, Part II, at 253.

eventually became section 1142 of the Bankruptcy Code, in the Commission's proposed bill, and in S. 2565, H.R. 10792, H.R. 31, and S. 236 all contained the following:

Carrying out the Plan. The debtor and any corporation organized or to be organized for the purpose of carrying out the plan shall comply with the provisions of the plan and with all orders of the court relative thereto and shall take all action necessary to carry out the plan, including obtaining the consent of any regulatory agency as to any rate change by a debtor that is a public utility. The debtor and any corporation organized for the purpose of carrying out the plan shall have full power and authority to take all action necessary to carry out the plan and the orders of the court notwithstanding any law or court decision or regulation of any regulatory agency of any state or subdivision thereof to the contrary, except that if the debtor is a public utility, the debtor or any successor corporation shall obtain the consent of any regulatory agency having jurisdiction over the debtor as to any rate change.

See, e.g., Commission Report, Part II, at 255-56 (emphasis added). The National Conference of Bankruptcy Judges proposal similarly provided, as to implementation, that:

the debtor and any corporation organized for the purpose of carrying out the plan shall have full power and authority to take all action necessary to carry out the plan and the orders of the court. Except for health, safety and zoning regulations, any law or court decision or regulation of any regulatory agency of any state or subdivision thereof to the contrary, except that if the debtor is a public utility, the debtor or any successor corporation shall obtain the consent of any regulatory agency having jurisdiction over the debtor as to any rate change.

H.R. 32, §4-706, 94th Cong., 1st Sess. (1975) (emphasis added).

Congress did not enact the foregoing language, although PSNH and the Committees are asserting positions as though Congress did. Congress had before it in numerous bills plain language which would have accomplished the result now urged by PSNH and the Committees, but Congress rejected that language. In fact, when one sees the proposition so baldly stated in the proposed statutory language, it is easy to see why the language was so quickly dropped from Congress' consideration in the bankruptcy reform process.

Congress' choice to eliminate this language is highly relevant in discerning congressional intent. Congress affirmatively rejected language which would have clearly accomplished the preemption that PSNH is suggesting Congress adopted. The reverse was true in Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 91 L.Ed. 1447 (1947). There, the court addressed state and federal laws regulating warehouses. A prior version of the federal legislation being considered had required federal license applicants to "secure the faithful performance of" state as well as federal warehousemen laws, and had further explicitly provided that the federal legislation would not be construed as limiting the effect of state warehousemen laws. Id. at 223. Both of those provisions were subsequently eliminated, and provisions were added stating that federal officials had exclusive power over federal license holders. This change in the

law was viewed as highly relevant by the Supreme Court. The change in the bankruptcy reform legislation which ultimately resulted in the Bankruptcy Reform of 1978 is similarly indicative of congressional intent here.

- D. The construction urged by PSNH is inconsistent with the deference which Congress has historically accorded to States in the regulation of utilities.

Since the early years of this century, the states have created comprehensive regulatory frameworks for the control of the activities of electric utilities. New Hampshire's public utility law was first enacted in 1911. See 1911 N.H. Laws 164. PSNH's construction of the Bankruptcy Code represents a radical departure from a consistent and long-standing policy of deference to such state regulation.

The history of federal legislation affecting electric utilities has been one of careful preservation of state regulatory authority and of supplementing state regulation with federal regulation in instances where state regulation by its nature was unable to protect the public interest. For example, the Public Utility Holding Company of 1935, 15 U.S.C. §79a-z (the "1935 Act"), was passed by Congress in response to the actions by multi-state holding companies, which were able to perpetrate abuses because state regulation of local utility subsidiaries did not reach the

holding companies themselves, the sources of abuse.

Specially, Congress found that:

...the interest of consumers of electric energy...are or may be adversely affected -

(2) when subsidiary public-utility companies are subjected to excessive charges for services, construction work, equipment, and materials, or enter into transactions in which evils result from an absence of arm's-length bargaining or from restraint of free and independent competition; when service, management, construction, and other contracts involve the allocation of charges among subsidiary public-utility companies in different States so as to present problems of regulation which cannot be dealt with effectively by the States;

(3) when control of subsidiary public-utility companies affects the accounting practices and rate, dividend, and other policies of such companies so as to complicate and obstruct State regulation of such companies, or when control of such companies is exerted through disproportionately small investment....

15 U.S.C. §79a(b).

With the 1935 Act, a statute with far-reaching consequences that had the effect of disintegrating the structure of the electric utility industry as it had developed, Congress preserved the regulatory authority of states. In determining the instances in which to allow exemptions from the registration provisions of the 1935 Act, two of the 1935 Act's exemptions are premised on the activities of the holding company and its electric utility's subsidiaries being confined to a single state. 15 U.S.C. §79c(1)&(2). With respect to the issuance of securities by registered holding companies, the 1935 Act provides:

(g) If a State commission or State securities commission, having jurisdiction over [the issuance of securities by utilities], shall inform the [Securities and Exchange] Commission, upon request by the Commission for an opinion or otherwise, that State laws applicable to the act in question have not been complied with, the Commission shall not permit a declaration regarding the act in question to become effective until and unless the Commission is satisfied that such compliance has been effected.

15 U.S.C. §79g(g).

Other examples of deferrals to state regulation are contained in Sections 8, 9 and 10 of the 1935 Act relating to the approval of certain transactions.*

8/ 15 U.S.C. §§79h, 79i & 79j. PSNH's "[Proposed] Disclosure Statement" relating to its reorganization plan (Document #2008) contains a glaring inconsistency in its position as to the effect of section 1123(a). On page 152, PSNH announces that it will comply with section 9(a)(2) of the 1935 Act, 15 U.S.C. §79i(a)(2) requiring prior approval of the Securities and Exchange Commission ("SEC") of the acquisition of utility securities if after the acquisition the acquirer would be an "affiliate" of more than one electric utility. The acquisition by the new holding company of the common stocks of Reorganized PSNH and DISCO is one of the key transactions by which PSNH proposes to implement its plan. It appears as well that the 1935 Act is a "non-bankruptcy law." Its conclusion that it must comply with this 1935 Act provision is wholly inconsistent with its position that it can disregard New Hampshire utility laws. Furthermore, in obtaining the requisite approval of the SEC, PSNH will be required to meet the standards of section 10 of the 1935 Act, which provides in part:

(f) The Commission shall not approve any acquisition as to which an application is made under this section unless it appears to the satisfaction of the Commission that such State laws as may apply in respect of such acquisition have been complied with, except where the Commission finds that compliance

(Footnote 8 continued on next page)

Furthermore, in section 11 of the 1935 Act relating to plans for the dissolution of holding companies, one primary standard for acceptance of such a plan is the confining of the resulting holding company system to a single state or one state and adjoining states -- again, to restore the effectiveness of state regulation rather than to supplant it. 15 U.S.C. §79k.

Congress also passed the Federal Power Act in 1935. 16 U.S.C. §791 et seq. The Federal Power Act regulated the transmission of electricity in interstate commerce and the rates for electric energy sold at wholesale. It was passed as a result of the Supreme Court's decision in Public Utilities Commission v. Attleboro Steam & Electric Co., 273 U.S. 83, 71 L.Ed. 549 (1927), in which the Court held that states are unable to regulate sales of electricity in interstate commerce. Congress acted to fill this void by enacting the Federal Power Act, while at the same time leaving regulation of intrastate retail electric service to the states. This stated policy is contained in section 201(a) of the Federal Power Act:

(Footnote 8 continued from previous page)

with such State laws would be detrimental to the carrying out of the provisions of section 11 [15 U.S.C. §79k] of this title. [The relevant provisions of section 11 do not apply to exempt holding companies].

15 U.S.C. §79j(f). PSNH concludes that it must comply with the 1935 Act. Therefore, PSNH is once again confronted with a Congressional requirement that state regulatory laws be obeyed.

(a) It is declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to subchapter III of this Chapter generation to the extent provided in this subchapter and the Part next and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

16 U.S.C. §824(a) (emphasis added).

Another example of the deference to the states is contained in section 204 of the Federal Power Act, which relates to FERC regulation of the issuance of securities by FERC-regulated utilities. Section 204(f) provides that:

The provisions of this section shall not extend to a public utility organized and operating in a State under the laws of which its securities issues are regulated by a State commission.

16 U.S.C. §824c(f).

A further example of the enhancement of state regulation is contained in the Public Utility Regulatory Policies Act of 1978, Pub. L. No. 95-617, 92 Stat. 3317 (codified as amended in various sections of 16 U.S.C.) ("PURPA"). Congress, in determining whether to implement various ratemaking standards, prescribed that such standards were to be considered by state commissions rather than imposed by federal authority, and provided in section 117(b) as follows:

State Authority. Nothing in this title prohibits any State regulatory authority or non-regulated electric utility from adopting, pursuant to State law any

standard or rule affecting electric utilities which is different from any standard established by this subtitle.

16 U.S.C. §2627(b).

In other sections of PURPA, such as section 205, which relates to power pooling laws, and section 210, which relates to co-generation and small power production facilities, provisions which preempt state law are carefully confined to meet specified federal policies with ongoing state participation in the process.

The 1935 Act, the Federal Power Act, and PURPA constitute the major examples of exercises of federal power in relation to the regulation of electric utilities. They demonstrate a consistent pattern by Congress to defer to the state regulatory process, even in the face of substantial federal interests. In most instances, they represent efforts by Congress to supplement rather than supplant state regulation, and in those instances in which state law is to be preempted, Congress' determination in that regard is express and precisely confined to implementation of the federal interest. Finally, in each instance it is clear that the objective is to protect the public interest rather than to ignore it.

This history of actions by Congress stands in stark contrast to the actions PSNH would have this Court believe Congress undertook in enacting the Bankruptcy Code in 1978, and in amending it in 1984.

CONCLUSION

The language of section 1123(a) of the Bankruptcy Code would, under the construction urged by PSNH and Committees, make the presiding judge in a chapter 11 case an exceptionally powerful chancellor. This extraordinary grant of power would be constrained only by the imagination of the plan proponent and the economic demands of creditors and equity security holders. Fundamental State interests would be abrogated and the influence of the public interest rejected.

Common sense suggests that such major realignment of federal and state authority and such a radical departure from pre-Code law would not be implemented without debate as to its wisdom as a matter of policy. See Shine v. Shine, 802 F.2d 583, 587-88 (1st Cir. 1986). Beyond common sense, this construction, as shown above, is contrary to the language of the Bankruptcy Code, when taken as a whole. It is inconsistent with the legislative history, which reflects congressional rejection of bills which would have accomplished the result now urged. It is contrary to the history of providing for the regulation of utilities by specially constituted, expert local administrative agencies rather than equity courts. It is contrary to the line of United States Supreme Court cases setting forth the rules for determining preemptive intent on the part of Congress. It

suggests a radical departure from pre-code law without any active consideration by Congress.

All of the indicia by which federal preemption is determined demonstrate that the construction of section 1123(a) urged by PSNH and the Committees is simply wrong. Public utility laws and the Bankruptcy Code can and do peacefully co-exist, just as they did under the Bankruptcy Act.

The State of New Hampshire respectfully requests this Court to deny the Motion for Summary Judgment of PSNH and render judgment in favor of the State.

Dated: May 30, 1989

Respectfully submitted,

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Attachment 2

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF
NEW HAMPSHIRE

PUBLIC SERVICE COMPANY OF
NEW HAMPSHIRE, a/k/a
"Public Service of
New Hampshire"
"PSNH"
"New Hampshire Yankee"
Debtor.

Chapter 11

Case No. 88-00043

PUBLIC SERVICE COMPANY OF NEW
HAMPSHIRE,

Adversary Proceeding
No. 89-08

Plaintiff,

v.

STATE OF NEW HAMPSHIRE and
STATE OF NEW HAMPSHIRE PUBLIC
UTILITIES COMMISSION,

Hearing Date: June 30, 1989
Time: 9:30 A.M.

Defendants.

REPLY MEMORANDUM OF OFFICIAL COMMITTEE OF UNSECURED
CREDITORS OF PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE
IN SUPPORT OF THE DEBTOR'S MOTION FOR SUMMARY JUDGMENT
DECLARING THAT §1123(a)(5) OF THE BANKRUPTCY CODE PREEMPTS
STATE LAW REQUIREMENTS FOR PUC APPROVAL OF ACTIONS TAKEN
TO IMPLEMENT THE DEBTOR'S PLAN OF REORGANIZATION

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INTRODUCTION

The Committee files this reply memorandum to respond to the arguments made by the State of New Hampshire (the "State"), in which it urges the Court to ignore the plain preemptive language of Section 1123(a)(5) of the Code and to adopt a tortured construction of this statutory provision which serves their particular interests in this case. This reply memorandum does not repeat the arguments made by the Committee in its primary brief, and reference is made to that Brief for a fuller exposition of the Committee's position and views.

A few features of the State's Memorandum are particularly noteworthy. First, the State runs away from the statutory language, preferring instead broad arguments of sound policy more appropriately addressed to Congress. Thus, the State contends that the policy favoring state regulation of public utilities outweighs competing bankruptcy policies, that it would be detrimental to the public interest to allow the preemption of state utility laws, and that such preemption would open up a Pandora's box of ill results. The State's focus on policy is understandable but the proper inquiry requires that the Court begin its search for the meaning of §1123(a)(5) by examining the statutory language and that it adhere to settled principles of statutory construction. One such principle is that if statutory

language is clear on its face, well-settled law permits the Court to proceed no farther.

In effect, the State urges that the Court rule in its favor on policy grounds. But the weighing of competing policy arguments is a distinctively legislative function and, therefore, the State's arguments are misdirected. Regardless of the Court's own policy views, and regardless of whether the Court believes Congress acted wisely by enacting §1123(a)(5), the Court is obligated to effectuate the intent manifested by Congress in the statutory language that Congress chose to enact. Since Congressional intent to preempt could hardly be clearer, the judicial task of statutory construction is well defined and the Court's latitude in the instant proceeding is circumscribed.

A second feature of the State's Memorandum is its apparent strategy of overwhelming its adversaries with the sheer number of its arguments. No argument is deemed by the State to be too weak or far-fetched to be worthy of mention. Although the Committee does not respond to each and every argument made by the State, the Committee's silence should not be construed as an admission with respect to any of the State's arguments.

I. WHERE CONGRESS HAS SPOKEN CLEARLY, ITS WILL MUST
BE RESPECTED, REGARDLESS OF WHETHER THE COURT
AGREES WITH THE LEGISLATION IT HAS ENACTED

The primary thrust of the State's argument addresses policy considerations rather than the explication of §1123(a)(5)

through principles of statutory construction. In essence, the State contends that Congress could not have meant to enact legislation granting reorganizing debtors the ability to disregard state law in implementing their plans of reorganization because this would be inimical to the public interest and contrary to sound policy. Thus, the State argues that "Congress did not empower a plan proponent to obviate legitimate and fundamental public interests." (State's Memorandum at 10); "these parties [the Debtor and the Committee] are asking the Court to accept ... that Congress chose for regulated enterprises such as PSNH to provide for their reorganization in total disregard of the public interest." (State's Memorandum at 12); "Congress did not set about usurping the legitimate exercise by the states and the federal government of valid police power laws." (State's Memorandum at 13). The State approaches the interpretation of §1123(a)(5) with the assumption that Congress did not enact legislation at odds with the State's own view of the public interest and sound policy, and proceeds to seek a way of construing §1123(a)(5) which is harmonious with its views and is beneficial to its interest in this case. This approach is not only methodologically unsound, but it also constitutes an implicit and improper request for the Court to shed its judicial robes and assume the legislative task of correcting what the State perceives to be a defective statute.

Methodologically, the State's result-oriented method of statutory construction is contrary to the well established principle of statutory construction requiring a court at the outset to focus solely on the language of the statute being construed, and to look to extraneous factors only where the statutory language contains some ambiguity. See United States v. Ron Pair Enterprises, Inc., 109 S. Ct. 1026, 1030 (1989); ("[W]here, as here, the statute's language is plain, the sole function of the courts is to enforce it according to its terms."); Blum v. Stenson, 465 U.S. 886, 896 (1984); Committee's Brief at 10-11. To approach the interpretation of §1123(a)(5) with the goal of furthering non-bankruptcy policies extraneous to the policies of the Bankruptcy Code necessarily renders such an exercise a de facto rationalization of a preordained conclusion, rather than an attempt to understand Congressional intent underlying §1123(a)(5). Furthermore, this approach improperly renders the federal bankruptcy policies subservient to other nonbankruptcy policies, contrary to the intent of Congress, as discussed below.

It is well established that policy arguments, such as those contained in the State's Memorandum, are irrelevant to the interpretation of an unambiguous statute. See, e.g., Badaracco v. Commissioner, 464 U.S. 386, 398 (1984) ("The question we must consider is whether the policy petitioners favor is that which Congress effectuated by its enactment of §6501. Courts are not

authorized to rewrite a statute because they might deem its effects susceptible of improvement."); Griffin v. Oceanic Contractors, Inc., 458 U.S. 564, 576 (1982) ("The remedy for any dissatisfaction with the results in particular cases lies with Congress and not with this Court. Congress may amend the statute; we may not."); In re Kelly, 841 F.2d 908, 913 (9th Cir. 1988) ("[P]olicy arguments are, of course, beside the point once Congress has spoken.")

Similarly, it is a fundamental principle of jurisprudence that "equity follows the law," Hedges v. Dixon County, 150 U.S. 182, 192 (1893); In re Shoreline Concrete Co., Inc., 831 F. 2d 903, 905 (9th Cir. 1987), and that "[c]ourts of equity are bound to follow express statutory commands to the same extent as are courts of law." Shoreline Concrete at 905. Thus, bankruptcy courts are not free to exercise their equitable powers to effectuate a policy or outcome which they deem desirable where this would be contrary to the dictates of Congress. See Norwest Bank Worthington v. Ahlers, 108 S. Ct. 963, 968-69, (1988) ("whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code."); United States v. Sutton, 786 F.2d 1305, 1308 (5th Cir. 1986) ("Section 105(a) ... does not authorize the bankruptcy courts to ... constitute a roving commission to do equity."). Moreover, the powers of the bankruptcy courts as courts of equity to consider the exigencies of particular cases may only be used

to further the federal bankruptcy policies and not to promote nonbankruptcy policies at the expense of the rehabilitation of debtors. NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984) ("The Bankruptcy Code does not authorize freewheeling consideration of every conceivable equity, but rather only how the equities relate to the success of the reorganization.").

Courts are bound to adhere to the dictates of a statute even when doing so will yield a result which had not been contemplated by Congress, if not contrary to Congressional intent. Even if the State were to persuade the Court that Congress had never given any thought to utility reorganizations when enacting §1123(a)(5) and, consequently, did not deliberately intend to preempt state utility laws in the context of plan implementation, this would be of no avail to the State. It is sufficient to sustain the position of the Committee and the Debtor on the federal preemption issue that Congress intended to enact a general rule which is applicable by its terms to the instant situation. As the court explained (U.S. Court and Patents Appeals): "if Congress made a choice of language which fairly brings a given situation within a statute, it is unimportant that the particular application may not have been contemplated by the legislators." Sears, Roebuck & Co., v. United States, 504 F.2d 1400, 1402 (1974) (Citing Barr v. United States, 324 U.S. 83, 90 (1945)).

In light of the above principles and authorities, the State's plea for this Court to weigh the public interest and policy considerations in rendering its decision on the federal preemptions issue must be rejected. Because the federal preemption issue is purely one of law, it is for Congress and not the courts to balance the equities. In enacting the Bankruptcy Code, Congress certainly considered the public interest and the relative importance of numerous competing policies and, after such consideration, decided to enact §1123(a)(5) which states that "notwithstanding any otherwise applicable nonbankruptcy law" a debtor may take certain actions to implement a plan. Congress thereby provided Chapter 11 debtors with a powerful tool to reorganize by freeing them from constraints which might otherwise frustrate numerous reorganization attempts. It is not a judicial function to second-guess this Congressional decision, nor to remedy its perceived defects.

II. POLICY CONSIDERATIONS FAVOR CONSTRUING §1123(a)(5)
IN ACCORDANCE WITH ITS PLAIN MEANING

A. Congress Has Accorded Great Importance to the
Rehabilitation of Debtors.

One of the primary purposes, if not the primary purpose, behind the enactment of Chapter 11 of the Bankruptcy Code, as well as of prior bankruptcy law, was to facilitate the rehabilitation of debtors. Thus, House Report No. 95-595, P.220 (1977) explains that "[t]he purpose of a business reorganization

case, unlike a liquidation case, is to restructure a business's finances so that it may continue to operate, provide its employees with jobs, pay its creditors, and produce a return for its stockholders." Congress went to great lengths in the drafting and enactment of the Bankruptcy Code to provide ample means to increase the likelihood of debtor rehabilitation, including providing, where appropriate, for the preemption of nonbankruptcy law. See e.g., §§363(1); 365(e)(1); 363(f)(1) and (3); 541(c)(1) and 1142(a).¹ Applicable court rulings reflect the Congressional emphasis on debtor rehabilitation, broadly construing the scope of applicable Bankruptcy Code provisions in order to effectuate this policy.

The leading ruling illustrating the importance of the Bankruptcy Code's debtor rehabilitation policy is NRLB v. Bildisco & Bildisco, 465 U.S. 513 (1984). In Bildisco, the Supreme Court addressed a conflict between the policies underlying the Bankruptcy Code and those of the National Labor Relations Act (NLRA). Despite a provision of the NLRA that an employer's refusal to bargain collectively with the representatives of his employees constituted an unfair labor practice, the Court held that: 1) collective bargaining

¹ An examination of the differing language of these provisions indicates that Congress clearly grasped the distinction between broad and narrow preemptive language, and when Congress sought to limit the preemptive effect of a particular provision it made this intent clear by identifying the type of nonbankruptcy laws which were subject to preemption.

agreements were executory contracts within the meaning of Code §365(a), subject to rejection if the debtor could show that they burdened the estate and that the balance of the equities favored rejection; and 2) a debtor does not commit an unfair labor practice when it unilaterally modifies or terminates one or more provisions of a collective bargaining agreement prior to court approval of the debtor's rejection of such agreement.

The focus of Bildisco's analysis was the Bankruptcy Code's reorganization policy. According to the Court, "the policy of Chapter 11 is to permit successful rehabilitation of debtors." 465 U.S. at 527.² Because the authority to reject burdensome contracts is critical to achieving this fundamental goal, to hold that the unilateral rejection of collective bargaining agreements constitutes an unfair labor practice would undermine the reorganization policy. At the same time, the Court recognized that due to the important national policy of avoiding labor strife, collective bargaining agreements are entitled to special deference, mandating that a debtor satisfy a higher than customary standard before rejecting a collective bargaining agreement. Nonetheless, the Court held that the policy favoring

² The court also stated:

The fundamental purpose of reorganization is to prevent a debtor from going into liquidation, with an attendant loss of jobs and possible misuse of economic resources.

Id. at 528.

preservation of collective bargaining agreements had to yield to the Code's provisions for the rehabilitation of debtors. According to the Court, to hold otherwise "would largely, if not completely, undermine whatever benefit the debtor-in-possession otherwise obtains by its authority to request rejection of the agreement." Id. at 528.

See also In re Charter Co., 862 F.2d 1500, 1502 (11th Cir. 1989) (Affirming the disallowance of a contingent claim for contribution and reimbursement pursuant to §502(e)(1)(B) of the Code, the Eleventh Circuit explained that §502(e)(1)(B) "epitomizes a considered Congressional policy that underlies the Bankruptcy Code as a whole ... [that] the debtor should be expeditiously rehabilitated and reorganized"); Moody v. Amoco Oil Co., 734 F.2d 1200, 1216 (7th Cir.) ("the purpose behind chapter 11 is to permit successful rehabilitation of debtors and to prevent a debtor from going into liquidation."), cert. denied, 469 U.S. 982 (1984); In re Monroe Well Service, Inc., 83 B.R. 317, 323 (Bankr. E.D. Pa. 1988); In re Security Gas & Oil, 70 B.R. 786, 795 (Bankr. N.D. Cal. 1987); In re Smith, 43 B.R. 313, 318 (Bankr. N.D. Ill. 1984); In re Gwinn, 34 B.R. 936, 945 (Bankr. S.D. Oh. 1985); In re Morris, 10 B.R. 448, 451 (Bankr. N.D. Iowa 1981), vacated in part, 21 B.R. 816 (Bankr. N.D. Iowa 1982). In light of the fact that promoting debtor rehabilitation is the most fundamental of all bankruptcy policies and forms the cornerstone of Chapter 11, the State's contention

that construing §1123(a)(5) in accordance with its plain terms runs contrary to sound public policy is clearly untenable.

Two Supreme Court rulings cited by the State in its Memorandum for the proposition that federal bankruptcy policies are of secondary importance to the protection of state interests, Kelly v. Robinson, 479 U.S. 36 (1986) and Midlantic National Bank v. New Jersey Department of Environmental Protection, 474 U.S. 494 (1986) (State's Memorandum at 39) are readily distinguishable from the situation at bar. The reorganization policy was not implicated in either Kelly or Midlantic because both cases involved liquidation proceedings under Chapter 7 of the Bankruptcy Code rather than Chapter 11 reorganizations. Consequently, these rulings fail to support the proposition urged by the State that the federal policy of encouraging the reorganization of debtors is secondary to the protection of important state interests.³ Moreover, Kelly and Midlantic are

³ Even if these rulings did support such a conclusion, which they do not, this would be insufficient to demonstrate that the reorganization policy is secondary to the particular state laws which are at issue in this proceeding, namely New Hampshire's public utility laws. It may not simply be assumed, in the absence of any evidence, that, New Hampshire's utility laws are entitled to the same degree of deference accorded to the particular environmental and criminal laws at issue in Midlantic and Kelly. Indeed, the Court's holding in Midlantic was a narrow one, expressly premised on its assessment of both the reasonableness of the state statute and the significance of the public interest involved. The Court stated:

[W]e hold that a trustee may not abandon property in contravention of a state statute or regulation that is reasonably designed to protect the public health or safety from identified hazards.

also distinguishable from the instant situation in that the provisions of the Bankruptcy Code which were being construed in those cases, §§523(a)(7) and 554(a), did not contain any preemptive language and, consequently, their interplay with state law was far more ambiguous than the relationship of §1123(a)(5) to New Hampshire's public utilities laws.⁴ This statutory ambiguity was noted by the Supreme Court subsequently in Ron Pair, wherein the Court stated that "[b]oth decisions concerned statutory language which ... was open to interpretation." Ron Pair at 1032-1033.⁵

Midlantic at 507.

* Thus, the Court in Kelly explained:

"On its face, §523(a)(7) certainly does not compel the conclusion reached by the Court of Appeals, that a discharge in bankruptcy voids restitution orders imposed as conditions of probation by state courts." Id. at 50.

⁵ A further significant reason why the Midlantic and Kelly holdings are inapposite to the federal preemption issue is that the consequence of preemption in those cases would have been to create a regulatory void; in other words, the state legislation that would have been displaced would not have been replaced by federal legislation in the same substantive area of law. By contrast, in the instant situation the preemption of the State's utilities laws will not leave the Debtor unregulated but, instead, will merely replace PUC regulation with substantially similar federal regulation. Because no regulatory void is created by §1123(a)(5) preemption of the State's utilities laws, the resulting harm to the public interest is either negligible or nonexistent.

B. State Police Power Laws Are Not Immune From Preemption.

The State in its Memorandum further argues that the straightforward statutory interpretation propounded by the Debtor and the Committee cannot be correct because it would result in the preemption of state police power legislation⁶. The State apparently would have the Court believe that state police power laws do not fall within the reach of the Supremacy Clause of the United States Constitution. Any such suggestion is absurd. Although state police power legislation which is challenged under the Supremacy Clause begins with a presumption of validity, where a conflict with federal legislation is demonstrated, laws enacted pursuant to a state's police powers are subject to preemption to the same extent as other state laws. See Ray v. Atlantic Richfield Co., 435 U.S. 151, 157 (1978); Association of American Medical Colleges v. Carey, 482 F. Supp. 1358, 1366 (N.D.N.Y. 1980) ("While there is generally an assumption that an exercise of state police powers, as claimed by defendants, is not preempted by a federal statute, a clear indication to do so cannot be ignored by the Court."). Although the instances in

⁶ For example, the State argues that "Section 1123(a)(5) contains no provision authorizing the plan proponent to utilize these 'means' to disregard valid state and federal police power laws in the confirmation of the plan." (State's Memorandum at 8); "PSNH and the Committees suggest that reorganization courts have boundless powers to ignore police power restrictions on the conduct of reorganizing enterprises." (State's Memorandum at 13).

which courts have ruled state police power laws to be invalid under the Supremacy Clause are too numerous to recount here, a few such rulings, including some involving the preemption of state laws regulating public utilities, are cited for illustrative purposes.

In Ray, the Supreme Court held that Washington statutes regulating the design, size and construction of oil tankers on Puget Sound, enacted pursuant to the police powers of that state, were invalid under the Supremacy Clause because they conflicted with the Ports and Waterways Safety Act of 1972 (33 U.S.C. 1221-1227; 46 U.S.C. 391a). Similarly, in Nantahala Power and Light Company v. Thornburg, 476 U.S. 953 (1986), the Supreme Court ruled that the North Carolina Utilities Commission's allocation of low cost power between two commonly owned electric utilities was preempted by the allocation of such power set by the Federal Energy Regulatory Commission. Recently, in Schneidewind v. ANR Pipeline Co., 485 U.S. 293 (1988), the Supreme Court ruled that a Michigan statute regulating the issuance of securities by public utilities which transport natural gas in that state was preempted by the Natural Gas Act (15 U.S.C. §717). See also Illinois v. General Elec. Co., 683 F.2d 206 (7th Cir. 1982) (Illinois Spent Fuel Act, which prohibited shipment of spent nuclear fuel into the state for storage, was preempted by Atomic Energy Act), cert. denied, 461 U.S. 913 (1983); Appalachian Power Co. v. Public Service Commission of West Virginia, 630 F.Supp. 656 (S.D.W.Va.

1986) (West Virginia Public Service Commission was preempted from granting or withholding its consent and approval to electric utility to enter into transmission agreement by Federal Power Act), Aff'd 812 F.2d 898 (4th Cir. 1987).

Preemption of state police power legislation by the federal bankruptcy laws is illustrated by In re Adelphi Hospital Corp., 579 F.2d 726 (2d Cir. 1978). In Adelphi, the Court of Appeals for the Second Circuit ruled that the New York State Department of Health could not require, pursuant to a New York statute, that the trustee of a hospital-debtor maintain and store patients' medical records. Although the court recognized that "[t]he State and the public obviously have a vital interest in the preservation of the bankrupt's hospital records," nonetheless the court explained that "[i]t is beyond peradventure that federal law prevails over inconsistent state laws." Id. at 729-730. See also, In re Continental Airlines Corp., 64 B.R. 858 (Bankr. S.D. Tex. 1986); In re Galbraith, 15 B.R. 549 (Bankr. E.D. Pa. 1981). The above rulings make it abundantly clear that state legislation is not immune from preemption merely because it is in the nature of police power legislation.

The State's attempt to carve out an exception from the Supremacy Clause for state police power laws suggests that the State believes that such laws are protected from preemption by

the Tenth Amendment of the United States Constitution,⁷ since only the Tenth Amendment is capable of preventing the preemption of state law by conflicting federal law pursuant to the Supremacy Clause. However, controlling court rulings leave no doubt that a Tenth Amendment challenge to federal preemption of New Hampshire's public utilities laws would not be a serious one. Over the past several years the Supreme Court has narrowed the scope of the protection afforded to the states by the Tenth Amendment, explaining in one key ruling that "the attempt to draw the boundaries of state regulatory immunity in terms of 'traditional governmental function' is not only unworkable but also inconsistent with established principles of federalism." Garcia v. San Antonio Metro Transit Auth., 469 U.S. 528, 531 (1985). Garcia and other leading rulings make abundantly clear that state regulation of public utilities is not immune from preemption merely because such regulation has historically been left to the states. See also, South Carolina v. Baker, 108 S. Ct. 1355, 1360 (1988) ("States must find their protection from congressional regulation through the national political process, not through judicially defined spheres of unregulable state activity.")

⁷ The Tenth Amendment provides as follows:

The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.

Accordingly, challenges to the Bankruptcy Code by states asserting violations of their Tenth Amendment rights have consistently been rejected. See In re Shroud Wholesale, Inc., 37 B.R. 735, 739 (Bankr. E.D.N.C. 1984) ("On several occasions when there has been a conflict between the powers of Congress to enact legislation to establish uniform laws on the subject of bankruptcies and the rights of the states under the Tenth Amendment, the Supreme Court recognized the paramount right of the United States Congress to enact uniform laws on the subject of bankruptcies." (citing Perez v. Campbell, 402 U.S. 637 (1971); Kalb v. Feurstein, 308 U.S. 433 (1940); and International Shoe v. Pinkus, 278 U.S. 261 (1929)), Reversed On Other Grounds, 47 B.R. 999 (E.D.N.C. 1985); In re Cropper Co., Inc., 63 B.R. 874, 876 (Bankr. M.D.Ga. 1986) (subordination of state tax liens pursuant to §724(b) of Code did not violate the Tenth Amendment); In re Galbraith, 15 B.R. 549, 557-58 ("federal interest in providing debtors with a fresh start in bankruptcy ... outweighs the state interest [in structuring a system of repayment by welfare recipients]"); Morris, supra, (discharge of debt for past alimony pursuant to 523(a) of the Code not barred by the Tenth Amendment).

III. THE STATE FAILS TO PROVIDE A PLAUSIBLE
INTERPRETATION OF §1123(a)(5) AND MISCONSTRUES
SEVERAL OTHER PROVISIONS OF THE CODE

A. The State Draws an Arbitrary Distinction Between
Various State Laws in an Attempt to Avoid the
Preemptive Effect of §1123(a)(5).

Relying primarily on policy arguments, the State's Memorandum fails to provide a plausible interpretation of the language of §1123(a)(5) and ignores the application of well established principles of statutory construction, discussed in the Committee's Brief, to this provision. Since the traditional and well established methods of statutory construction do not serve the State's ends, the State instead attempts to force its desired interpretation upon the language of §1123(a)(5), imposing upon it concepts which its words will not bear, and then, in order to maintain the semblance of a coherent statutory structure, misconstruing several interrelated provisions of the Code.

Even the State does not go so far as to dispute that the "notwithstanding" clause of §1123(a)(5) is of preemptive import, since such a position would do violence to the English language and would be patently absurd. Instead, the State attempts to blunt the preemptive effect of §1123(a)(5) by reading into it limitations that have no basis in either the language of §1123(a)(5) or elsewhere in the Bankruptcy Code. According to the State, the preemptive language of §1123(a)(5) was intended only "to avoid the application of contractual and other non-

bankruptcy law rights of creditors and equity security holders to prevent the inclusion of methods to resolve equitably their conflicting claims through the distribution of value under reorganization plans." (State's Memorandum at 16.) For example, the State suggests that §1123(a)(5) would preempt non-bankruptcy corporate laws requiring shareholder votes as a prerequisite to dissolution, merger and the sale of assets outside the ordinary course of business. Thus, the State offers an extremely narrow interpretation of the scope of §1123(a)(5)'s preemption, claiming that §1123(a)(5) supercedes corporate governance laws, but no other state laws.

The sole basis for the State's narrow construction of §1123(a)(5) is that such interpretation comports with its policy views. However, the statutory language draws no distinction between corporate governance laws and other nonbankruptcy laws, just as it draws no distinction between police power legislation and other state laws. Indeed, the language of §1123(a)(5) is directly at odds with the State's interpretation, since §1123(a)(5) by its plain terms preempts "any" otherwise applicable nonbankruptcy law and not merely some particular nonbankruptcy laws. If Congress had intended to limit the scope of §1123(a)(5)'s preemption in the manner suggested by the State it undoubtedly would have made this intent clear by identifying the type of legislation it sought to preempt, as it did in other provisions of the Code. See, e.g., §363(e), 365(f) and 1142(a).

Absent some compelling reason, it should not simply be assumed that Congress' choice of the phrase "any...nonbankruptcy law" is attributable to an oversight of the drafters or to poor draftsmanship; if the language used by Congress can casually be attributed to poor draftsmanship then it is never a guide to Congressional intent, and all statutory construction is an exercise in futility.

Moreover, even if the State's narrow construction of §1123(a)(5) were correct, this would be of little benefit to the State because the type of State legislation which is at issue in the proceeding at bar is in the nature of corporate governance legislation, which the State acknowledges is subject to preemption. Those State laws which are implicated by the Debtor's Plan all pertain to matters of corporate governance - i.e. the issuance of securities, the transfer and disposition of assets and the formation of subsidiaries and other affiliate corporations by public utilities. Consequently, even under the State's construction of §1123(a)(5), this provision obviates the need to obtain those PUC approvals which would be required outside of bankruptcy in order to effectuate the restructuring contemplated in the Debtor's Plan (or any other plan which may be filed that similarly relies upon §1123(a)(5)).

B. Section 1129(a)(6) Limits The Role of Regulatory Authorities in Utility Reorganizations, and is not a Feasibility Provision.

As discussed more fully in the Committee's Brief (at 23-24), it is apparent from §1129(a)(6) of the Code, which grants to regulatory agencies the authority to approve or disapprove any rate change provided in a debtor's plan of reorganization, that when Congress sought to grant authority concerning the plans of utility-debtors to regulatory agencies it did so in plain language. Application of the principle of expressio unius est exclusio alterius to the clear expression of Congressional intent found in §1129(a)(6) and the total absence of any similar language elsewhere in Chapter 11, compels the conclusion that Congress intended to limit the powers of state utility commissions in the plan process to those set forth in §1129(a)(6).

Although the State does not dispute the validity of the expressio unius principle, the State attempts to escape its application by arguing that "§1129(a)(6) is a specific feasibility provision relating to public utility debtors, and no more." (State's Memorandum at 20.) The State's position is that the purpose of §1129(a)(6) is to insure that any rate change built into a plan be found by the appropriate agency to be adequate to sustain the reorganized utility-debtor through the generation of sufficient revenue. By adopting this interpretation of §1129(a)(6) the State seeks to avoid the

conclusion that Congress deliberately declined to grant regulatory commissions the authority to approve acts incident to corporate restructurings, since if this were not so, Congress would have expressly granted commissions such authority, just as Congress expressly provided for regulatory jurisdiction over a utility-debtor's rates.

The State's novel interpretation of §1129(a)(6) must be rejected for at least two reasons. First, as the State reminds us on several occasions, interpretation of the Bankruptcy Code is a "holistic" endeavor (State's Memorandum at 8, 9, 14, and 23). Section 1129 of the Code already contains a separate feasibility requirement for plan confirmation (§1129(a)(11)) which applies to public utility-debtors as well as to all other Chapter 11 debtors; consequently, it would have been redundant for Congress to enact §1129(a)(6) simply in order to establish a feasibility requirement for utility-debtors.

Second, it has never been the function of any state public utility commission to pass on a proposed rate change solely from the perspective of the regulated utility in order to guarantee the utility an adequate return. Rather, the mandate of such commissions when considering a proposed rate change is to weigh both the utility's need for an adequate return and the consuming public's need for affordable rates. Section 1129(a)(6) does not direct public utility commissions to deviate from this mandate. However, the State's interpretation of §1129(a)(6)

would impose upon public utility commissions the responsibility of assuring the adequacy of a utility-debtor's revenues and thereby transform their role from neutral parties as between utility commissions and their consumers to allies of utility-debtors; surely no one who is familiar with this case can imagine the PUC acting in this capacity.

For these reasons, it is abundantly clear that, rather than being a feasibility provision, §1129(a)(6) was intended to grant authority to regulatory commissions to approve or disapprove rate changes contained in the reorganization plans of utility debtors. Congress' concomittant failure to grant regulatory commissions the power to disapprove those acts by utility-debtors pertaining to corporate restructurings, expressly set forth in §1123(a)(5), reflects a deliberate decision by Congress to deny this power to regulatory commissions in order to afford utility-debtors the same opportunity to reorganize as other Chapter 11 debtors.

Significantly, §1129(a)(6) requires approval of a rate change provided for in a plan only from the regulatory commission "with jurisdiction, after confirmation of the plan, over the rates of the debtor." (emphasis supplied). The requirement that approval be obtained from the regulatory body with postconfirmation jurisdiction over a debtor's rates rather than from the commission with jurisdiction prior to confirmation, represents a major departure from pre-Code policy. Sections 177

and 178 of the former Bankruptcy Act, which governed public utility reorganizations under the Act, required the approval only of those commissions which regulated a debtor prior to confirmation, making no mention whatsoever of commissions with postconfirmation jurisdiction.

This change, effected by the insertion of explicit language referring only to commissions with postconfirmation jurisdiction, could not have been accidental. Rather, it indicates that Congress specifically contemplated and sanctioned the possibility that confirmation of a utility-debtor's plan would effect a change in the manner in which such a debtor would be regulated subsequent to confirmation. In light of this clear manifestation of Congressional intent that a plan could cause a change in the commission with regulatory jurisdiction over a utility-debtor, the State's assertion that §1123(a)(5) would not have been intended to achieve this result is plainly incorrect. Congress, when it enacted the Bankruptcy Code, foresaw the possibility of plans, such as the Debtor's, effecting a change in regulatory jurisdiction, sanctioned their validity, and provided §1123(a)(5) as the means to implement such plans.

C. Preemption of Nonbankruptcy Law in the Context of Plan Implementation is Governed by §1123(a)(5), Not by §1142(a) and §363(1).

According to the State, the scope of the Bankruptcy Code's preemption of nonbankruptcy law in the context of plan

implementation is governed by §1142(a) of the Code, rather than by §1123(a)(5) (State's Memorandum at 22-23); unlike §1123(a)(5) which preempts "any" nonbankruptcy law, §1142(a) provides for the preemption of only nonbankruptcy laws "relating to financial condition." Thus, the State effectively seeks to take shelter under the more narrow preemptive language of §1142(a) and thereby to escape the broader preemption of §1123(a)(5).

The State's interpretation of §1142(a), like that of several other provisions of the Code, is erroneous. Had the State sought to construe §1142(a) as part of a "holistic endeavor" (State's Memorandum at 23), it would have immediately realized that Chapter 11 of the Code is comprised of four distinct Subchapters, which are so designated,⁸ and which pertain to completely different aspects of a Chapter 11 case. Section 1123 belongs to Subchapter II, titled The Plan, which pertains to the plan confirmation process and sets forth, among other things, who may file a plan and when (§1121); principles for classification of claims and interests in a plan (§1122); the contents of a plan (§1123); and the standards for plan confirmation (§1129). Section 1123(a)(5) is part of a section dealing with (and titled) the contents of a plan and, accordingly, is the only section in Chapter 11 that sets forth

⁸. Subchapter I, §§1101 through 1114, is titled Officers and Administration; Subchapter II, §§1121 through 1129, is titled The Plan; Subchapter III, §§1141 through 1146, is titled Postconfirmation Matters; and Subchapter IV, §§1161 through 1174, is titled Railroad Reorganization.

criteria for what may be included in a Chapter 11 plan. Significantly and dispositively, §1123(a)(5) provides that a Chapter 11 plan must provide adequate means for the plan's implementation, and that such means of implementation may include certain acts without regard to the restrictions or prohibitions imposed by otherwise applicable nonbankruptcy law. Public utility-debtors are not excluded from the right to avail themselves of this powerful rehabilitative tool.

By contrast, §1142(a) belongs to Subchapter III, entitled Postconfirmation Matters, and, accordingly, deals not with the substantive provisions of a plan but, rather, with the effectuation of a confirmed plan. See, Goodman v. Phillip R. Curtis Enterprises, Inc., 809 F.2d 228, 232 (4th Cir. 1987) (Section 1142(a) constitutes a "grant of postconfirmation authority...concerning the implementation of a confirmed plan."); In re Paradise Valley Club, 26 B.R. 990, 992 (Bankr. D. Colo.), Aff'd, 31 B.R. 613 (D. Colo. 1983). Unlike §1123(a)(5) which expands a debtor's preconfirmation rights⁹ and gives the debtor a powerful tool for reorganizing, §1142(a) does not confer rights but rather is an enforcement provision imposing an affirmative duty upon the debtor to carry out the provisions of a confirmed

⁹ As the Fourth Circuit explained in In re FCX, Inc., 853 F.2d 1149, 1155 (4th Cir. 1988): " §1123(a)(5) is an empowering statute. ... Section 1123(a)(5) ... does not simply provide a means to exercise the debtor's prebankruptcy rights; it enlarges the scope of those rights", cert. denied, 109 S. Ct. 1118 (1989).

plan. See, e.g., In re Sonner, 53 B.R. 859 (Bankr. E.D. Va. 1985) ("both Sonner and the Creditors Trust have the duty and responsibility of carrying out the plan." (citing §1142(a))).

In accordance with its function of furthering the effectuation of a confirmed plan, §1142(a) has been construed by several courts as a jurisdictional provision that preserves the authority of a bankruptcy court after confirmation to issue such further orders as may be necessary to aid in implementation of a plan. See, e.g., In re Cinderella Clothing Industries, Inc., 93 B.R. 373, 379 (Bankr. E.D. Pa. 1988) ("§1142 gives the court the power to enforce debtor compliance with plan terms, ... and to prevent third parties from interfering with the consummation of the plan.") (citation omitted); Paradise Valley, 26 B.R. at 992, ("Section 1142(a) in particular, necessarily impl[ies] some retention of jurisdiction in the bankruptcy court, at least with respect to execution of the confirmed plan.")¹⁰ Thus, it is clear that §§1123(a)(5) and 1142(a) serve distinct functions in the scheme of the Bankruptcy Code, and that §1123(a)(5), which delineates the substantive provisions of a plan, governs the scope of the acts which may be provided for in a plan and their relationship with nonbankruptcy law; accordingly the acts provided for in a plan are governed by the broad preemption of §1123(a)(5) rather than the narrower preemption of §1142(a).

¹⁰ Collier also titles its discussion of §1142(a) "Jurisdiction of the Court."

The State further argues that §363(1)¹¹ of the Code, as well as §1142(a), defines the scope of Bankruptcy Code preemption in connection with plan implementation. (State's Memorandum at 25.) According to the State, this must be so because the interpretation of §1123(a)(5) propounded by the Debtor and the Committee renders superfluous the preemptive language of §363(1), which also involves the disposition of property pursuant to a plan. This argument is plainly incorrect because the scope of §363(1) is much broader than the context of a Chapter 11 plan. Section 363(1) authorizes the disposition of property both pursuant to a plan and outside of a plan and, moreover, is also applicable to cases under Chapters 12 and 13 of the Bankruptcy Code. Therefore, it is clear that the broad preemption of §1123(a)(5), which is limited to Chapter 11 plans, does not render the narrower preemption of §363(1) superfluous. It is also clear that §363(1) has only a very limited application to plan implementation, since it concerns only a few of the means of implementation set forth in §1123(a)(5).

D. The State Ignores Well Established Principles of Statutory Construction, and Fails to Respond to the Arguments Raised in the Committee Brief.

Notwithstanding the State's misinterpretation of the numerous Code provisions discussed above, perhaps the most

¹¹ Section 363(1) preempts certain ipso facto clauses which, if not for such preemption, would terminate or modify a debtor's interest in property of the estate.

telling sign of fallacies of the State's interpretation of §1123(a)(5) is the State's failure to offer any response to the dispositive statutory construction arguments contained in the Committee's Brief. Significantly, the State does not attempt to demonstrate that there is any ambiguity in the language of §1123(a)(5) that would require the Court to resort to extraneous sources to assist its interpretation of this provision; instead, the State simply makes a blanket and unsupportable assertion that this is the case (State's Memorandum at 31). However, such a blanket assertion is inadequate to blunt the effect of Ron Pair and several other Supreme Court rulings that require a court to look no farther than the language of a statute when such language is plain and unambiguous (See cases cited in Committee Brief at 10-11). The State's attempt to create an ambiguity by looking to other provisions of the Code (and misconstruing these provisions) is inherently circular, since it is inappropriate to rely on these provisions in the first instance, given the unambiguous language of §1123(a)(5).

Additionally, and equally importantly, the State totally ignores the fundamental principle of statutory construction, expressio unius est exclusio alterius (the expression of one thing is the exclusion of another). The State fails to offer any response whatsoever to the several applications of this canon of construction discussed in the Committee Brief (at 23-31), including: 1) the presence in the

Bankruptcy Code of an express provision requiring railroad debtors seeking to transfer assets pursuant to a plan to obtain applicable regulatory approval, coupled with the absence of any similar requirement for utility-debtors; 2) the inclusion in Chapter 9 of the Code of a provision requiring, as a condition to the confirmation of a plan of a municipality-debtor, that all regulatory approvals applicable outside of bankruptcy be obtained, coupled with the absence of any such requirement for utility-debtors; and 3) Congress' deliberate decision not to carry over to the Bankruptcy Code provisions contained in the former Bankruptcy Act which granted regulatory commissions broad authority over a utility-debtor's plan of reorganization, nor to continue the involvement of regulatory commissions at all in the reorganization process, other than as provided in §1129(a)(6). The State's failure to respond to these powerful arguments is susceptible of only one interpretation, namely that there is no response to them.

E. The Inapplicability of Certain Code Provisions to Regulatory Agencies Does not Exempt These Agencies From The Express Directives of Other Code Provisions.

The State advances the curious argument that because regulatory agencies are not treated under sections 1124 through 1128 of the Code, therefore Congress could not have intended for such agencies to be subject to §1123. (State's Memorandum at 17-18.) Although the basis of this argument is unclear, even a cursory examination of Code sections 1124 through 1128 reveals

that these provisions are inherently inapplicable to parties, such as regulatory agencies, which are not treated under a plan. Since there is no sensible reason why regulatory authorities should be treated under these sections of the Code, it is illogical to suppose that this exclusion demonstrates a similar Congressional intent to exclude regulatory authorities from other, completely different, Code provisions that ought to be applicable to them. Moreover, the State's argument is inconsistent with its position that §1123(a)(5) is applicable to, and preempts, state corporate governance laws, since states are not treated under sections 1124 through 1128.

IV. RESPONSE TO MISCELLANEOUS ARGUMENTS

We respond briefly for the State's other scattershot contentions.

A. The Debtor's Plan is not Proposed "By Means Forbidden By Law".

The State certainly is clutching at straws when it adduces as a ground for rejecting the plain meaning of §1123(a)(5), the argument that this interpretation is at odds with §1129(a)(3) of the Code (which requires as a condition to confirmation that a plan has been "proposed in good faith and not by any means forbidden by law"). According to the State, the Committee's interpretation of §1123(a)(5) must be incorrect

because otherwise the Debtor would be permitted to file a plan that proposes to take actions forbidden by law, in violation of §1129(a)(3). (State's Memorandum at 18-20.) This argument is obviously circular, since it assumes as its premise that the actions proposed in the Debtor's Plan are forbidden by law - the very issue which the instant adversary proceeding is intended to decide. If the Court rules in favor of the Debtor and the Committee on the federal preemption issue, then the State's premise will be proven incorrect.

Furthermore, as the State comes close to acknowledging, §1129(a)(3) is concerned with the process of soliciting acceptances of a plan and has nothing to do with the substantive provisions of a plan. See, In re Sovereign Group, 1984-21, Ltd., 88 B.R. 325 (Bankr. D. Colo. 1988) ("the focus of §1129(a)(3) is upon the conduct manifested in obtaining the confirmation votes . . . and not necessarily on the substantive nature of the plan." (Citing 5 Collier, ¶1129.02 (15th Ed. 1984))). Therefore, §1129(a)(3) is completely inapposite to the interpretation of §1123(a)(5).

B. The State Distorts The FCX Holding.

According to the State, notwithstanding that the Fourth Circuit in In re FCX, Inc., 853 F.2d 1149 (4th Cir. 1988), ruled on precisely the issue presently before the Court, namely the proper interpretation of §1123(a)(5), such ruling is, amazingly,

"inapplicable" to the proceeding at bar. (State's Memorandum at 22.) The reason offered by the State for its casual dismissal of the leading ruling concerning §1123(a)(5) is that in FCX it was "section 1141 that created the preemptive effect found by the Fourth Circuit." The State is undeterred from propounding this novel reading of FCX by the fact that §1141 was not implicated in the court's ruling and, indeed, was not even mentioned in the Fourth Circuit's entire opinion.

The State's attempt to rely on §1141 of the Code reflects a confusion on its part between the binding effect of a confirmed plan on holders of claims and interests pursuant to §1141, on the one hand, and the preemptive effect of federal legislation on state laws, on the other. Unlike creditors and interest holders who are bound, by virtue of §1141, to the terms of a confirmed plan, the State and the PUC are not so bound, but, nonetheless they may be impacted by a plan. Section 1141 by its terms does not purport to guarantee that entities not bound by a plan will not be effected by such plan, nor to assure state laws an immunity from preemption. Indeed, the State admits that corporate governance laws are subject to preemption by the

Bankruptcy Code, notwithstanding that states are not bound by a plan pursuant to §1141.

- C. The Language Which Congress Chose To Enact Reveals Far More About Congressional Intent Than The Language of Legislation Which was not Enacted.

The State attempts to demonstrate that Congress could not have intended in §1123(a)(5) to preempt applicable nonbankruptcy regulatory laws in the context of plan implementation by pointing out that, several years prior to enactment of the Bankruptcy Code, Congress declined to enact legislation of similar import. (State's Memorandum at 53-57.) However, just as the Supreme Court has explained that "the views of a subsequent Congress form a hazardous basis for inferring the intent of an earlier one," Consumer Product Safety Com'm v. GTE Sylvania, Inc., 100 S. Ct. 2051, 2061 (1980); United States v. Price, 361 U.S. 304, 313 (1960), so too the views of an earlier Congress may not be attributed to a later one. While no one, including the State, knows exactly why Congress declined to enact the proposed legislation cited by the State, the legislation which Congress did choose to enact is clear on its face that Congress intended to preempt any nonbankruptcy laws which restrict a debtor's ability to undertake acts expressly authorized by §1123(a)(5). Mere speculation concerning why Congress chose not to enact legislation many years ago is

insufficient to negate a clear manifestation of Congressional intent through legislation that is currently in force.

In light of the fact that the Congressional decision not to enact the proposed legislation cited by the States was made several years prior to the enactment of the Bankruptcy Code in 1978, the relevance of this decision to the stipulation of §1123(a)(5) is, at best, questionable. However, it would hardly be surprising to find, as frequently happens, that the proposed legislation, which was unable to garner sufficient interest or support upon first being proposed eventually succeeded in winning passage years later; thus, the proposed legislation to which the State refers may have been the forbearer of §1123(a)(5). In any event, the proposed legislation clearly indicates that for several years prior to the enactment of the Bankruptcy Code, Congress had considered granting debtors (and other plan proponents) expanded powers to implement plans of reorganization and that it was no accident when Congress finally enacted legislation containing language which plainly expressed this intent.

D. No Inference Concerning Congressional Intent
May be Drawn From the Absence of any Legislative
History Explaining the Purpose of §1123(a)(5)

The State attaches great significance to the silence of the legislative history to §1123(a)(5) of the Bankruptcy Code concerning Congressional intent in enacting this provision.

(State's Memorandum at 45.) According to the State, if Congress has intended the enactment of the Bankruptcy Code to effect a substantive change with respect to the preemption of state utility law in the context of plan implementation, it would have said so explicitly in the legislative history. However, the State errs in assuming that the legislative history to the Bankruptcy Code was intended to serve as a detailed commentary on each and every provision of the Code. As the Supreme Court recently explained with respect to the enactment of the Bankruptcy Code in Ron Pair, "[i]n such a substantial overhaul of the system, it is not appropriate or realistic to expect Congress to have explained with particularity each step it took." 109 S. Ct. at 1030.

In Ron Pair, notwithstanding the absence of any legislative history to §506(b) of the Code indicating that Congress intended to effect a change in the pre-Code rule disallowing postpetition interest on oversecured claims where the lien was nonconsensual, the Court nevertheless ruled that the enactment of §506(b) was intended to alter this rule. According to the Court, the absence of any legislative history indicating Congressional intent to effect a change was immaterial because "as long as the statutory scheme is coherent and consistent, there is generally no need for a court to inquire beyond the plain language of the statute." Id. The same principles are applicable in the instant proceeding; since, as demonstrated in

the Committee's Brief, the language of §1123(A)(5) is straightforward and the statutory scheme of the Bankruptcy Code is, under the Committee's interpretation, coherent and consistent, it is unnecessary for the Court to look beyond the plain language of §1123(a)(5).

Indeed, the interpretation of §1123(a)(5) presents a more compelling case for the Court to find that Congress intended to effect a change in pre-Code policy than the interpretation of §506(b), since there are other telltale signs of such Congressional intent. As discussed in the Committee's Brief, by omitting from the Code detailed provisions concerning utility reorganizations contained in the former Bankruptcy Act, Congress left little doubt of its intention to change pre-Code policy with respect to the role of regulatory commissions in utility reorganizations. In addition, the proposed legislation discussed above concerning the preemption of nonbankruptcy law in the context of plan implementation indicates that the change effected by §1123(a)(5) had been contemplated by Congress for some time.

E. The Committee Does Not Suggest That A Reorganizing Debtor May Disregard All Civil and Criminal Laws.

The State repeatedly attributes to the Debtor and the Committee the view that "in order to maximize value for the purpose of reorganizing a debtor, every law outside of the Bankruptcy Code, state or federal, civil or criminal, can be brushed aside by the reorganizing debtor." (State's Memorandum

at 31; also at 13 and 63.) The Committee does not and never has espoused this view.

Contrary to the parade of horrors conjured up by the State, the entire panoply of federal and state legislation would not fall by the wayside if the Debtor and the Committee were to prevail on the federal preemption issue. Rather, the only legislation subject to preemption under §1123(a)(5) is that which governs the acts authorized pursuant to this provision, all of which are connected with corporate restructurings. This clearly excludes, among other things, the entire body of criminal law (except insofar as the violation of certain corporate governance laws is statutorily deemed to be a criminal offense).

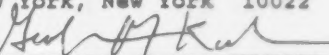
Nor would a ruling as urged in this Memorandum lead to a complete disruption of the regulatory process, as the State suggests, since no regulatory void will result from the preemption pursuant to §1123(a)(5) of the State's public utilities laws. Rather, State regulation of the Debtor would simply be replaced by a substantially similar and equally competent scheme of federal regulation with no net detriment to the public interest. Consequently, were the Court to rule that the Debtor and the Committee have correctly construed §1123(a)(5), the implications of this ruling would be far narrower than the State would have the Court believe.

CONCLUSION

For the reasons discussed above, the Court should grant summary judgment for the Debtor upon the Declaratory Judgment Complaint.

Dated: New York, New York
June 14, 1989

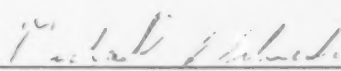
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By: 
A Member of the Firm2

Certificate of Service

I, Michael S. Schneider, an associate at the firm of Kramer, Levin, Nessen, Kamin & Frankel, certify that I caused to be served on June 15, 1989 by regular mail upon all parties appearing on the Short List updated as of May 12, 1989, and by Federal Express upon the Debtor, its counsel, the United States Trustee, the Examiner and his counsel, the office of the Attorney General of the State of New Hampshire and its counsel, and counsel for and each member of the official committees appointed pursuant to 11 U.S.C. §1102(a), a true copy of the following:

Reply Memorandum of Official Committee of Unsecured Creditors of Public Service Company of New Hampshire in Support of the Debtor's Motion for Summary Judgment Declaring that § 1123 (a)(5) of the Bankruptcy Code Preempts State Law Requirements for PUC Approval of Actions Taken to Implement the Debtor's Plan of Reorganization.


MICHAEL S. SCHNEIDER

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726 FEDERAL REPORTER, 2d SERIES

In the Matter of Eugene L. REYNOLDS,
Elaine M. Reynolds, Alan Eugene Lind-
ner, Michael A. Miltimore, Rosalie A.
Miltimore, Robert S. Winterfeld, Debt-
ors.

STATE OF IDAHO, DEPARTMENT OF
HEALTH & WELFARE,
Plaintiff-Appellant,

v.

Eugene L. REYNOLDS, Alan Eugene
Lindner, Michael A. Miltimore, Robert
S. Winterfeld, Defendants-Appellees,

In the Matter of James E. HAZEN,
Sherry Hazen, Debtors.

STATE OF IDAHO, DEPARTMENT OF
HEALTH & WELFARE,
Plaintiff-Appellant,

v.

James E. HAZEN, Defendant-Appellee.

Nos. 83-3571, 83-3572.

United States Court of Appeals,
Ninth Circuit.

Argued and Submitted Oct. 13, 1983.

Decided Feb. 28, 1984.

State appealed from an order of the Bankruptcy Court, 19 B.R. 545, which held that certain child support obligations which mothers had assigned to the states were dischargeable in fathers' bankruptcy proceedings. The District Court for the District of Idaho, Harold L. Ryan, J., 26 B.R. 181, affirmed. The Court of Appeals, Alarcon, J., held that amendment to Bankruptcy Code making such obligations nondischargeable was applicable to bankruptcy proceedings which were pending on the effective date of the statute.

Reversed and remanded.

Wallace, Circuit Judge, filed a concurring opinion.

1. Bankruptcy $\Rightarrow$ 467(4)

Question of whether dischargeability of child support obligations should be determined by law in effect on the date of the filing of the petition in bankruptcy or on the date of the ruling by the judge on the issue is a question of law subject to de novo review by the Court of Appeals.

2. Constitutional Law $\Rightarrow$ 186

Retroactive application of a federal statute other than an ex post facto law or a bill of attainder is not forbidden under the Constitution so long as due process requirements are met.

3. Federal Courts $\Rightarrow$ 924

As a general rule, judge should apply the law in effect on the date of the decision.

4. Statutes $\Rightarrow$ 262

Legislation is not applied to pending cases where Congress has expressly directed that the law is prospective only or where manifest injustice would result from a retrospective application.

5. Bankruptcy $\Rightarrow$ 6

Amendment to Bankruptcy Code providing that child support obligation owed to state agency as the result of the mother's assignment is not dischargeable in bankruptcy was to be applied to bankruptcy cases which were pending on the effective date of the amendment. Bankr.Code, 11 U.S.C.A. § 523(a)(5)(A).

Christopher D. Bray, Bray & Bernter, Boise, Idaho, for plaintiff-appellant.

William Breck Seiniger, Jr., Boise, Idaho, for defendants-appellees.

Appeal from the United States District Court for the District of Idaho.

Before WALLACE, ALARCON and BOOCHEVER, Circuit Judges.

ALARCON, Circuit Judge:

We must decide whether an amendment to 11 U.S.C. § 523(a)(5)(A), effective August 13, 1981, applies to pending bankruptcy cases in which the debtor filed a petition before that date. The district court, 26

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Cite as 726 F.2d 1420 (1984)

B.R. 181, held that the amendment should not be given retroactive effect and applied the law in effect as of the date of the filing of the bankruptcy petition. We reverse.

I.

The district court consolidated the cases of five individual debtors: Hazen, Reynolds, Miltimore, Winterfeld, and Lindner. There are common factual elements.

All five individuals were divorced from their spouses pursuant to Idaho court judgments, which awarded custody of their minor children to the wives and specific amounts of child support per month. The women applied for and received monthly public assistance payments from the State of Idaho, Department of Health and Welfare, for the benefit of their minor children. The women assigned their rights to receive child support payments to the state.

Some of the debtors filed bankruptcy petitions, seeking in part to discharge their child support obligations. In other cases, the State of Idaho filed suit pursuant to state law to collect delinquent child support payments and received a judgment awarding the state the unpaid child support, attorneys' fees, costs and statutory interest. The debtors then filed their bankruptcy petitions.

After the filing of these bankruptcy petitions, Congress amended 11 U.S.C. § 523(a)(5)(A) to disallow the discharge of a child support obligation assigned to an entity under section 402(a)(26) of the Social Security Act, which requires an applicant for assistance under the Aid to Families with Dependent Children program (AFDC) to assign child support obligations to the state administering the program. The amendment was made effective August 13, 1981. After this date, the bankruptcy court granted each of the debtors a discharge. The State of Idaho filed objections to the discharge of the child support obligations.

The bankruptcy court held in *Matter of Hazen*, 19 B.R. 545 (Bkrtcy.D.Idaho 1982), that dischargeability of the child support obligations assigned to the state should be determined by the law in effect at the time

of the filing of the debtor's petition in bankruptcy. Therefore, the debts were dischargeable. The cases of Hazen and Reynolds were decided together; those of Miltimore, Winterfeld, and Lindner were decided on the basis of *Hazen*. The district court affirmed the decisions of the bankruptcy judge.

II.

[1] Whether the dischargeability of child support obligations should be determined by the law in effect on the date of the filing of the petition in bankruptcy or on the date of the ruling by the judge on the issue is a question of law subject to *de novo* review by this court. The facts have been stipulated by the parties. See *Matter of B & W Enterprises, Inc.*, 713 F.2d 534, 536 (9th Cir.1983) (stipulated facts, remaining questions of law subject to *de novo* review).

In 1974 Congress enacted legislation that prohibited the discharge of child support obligations assigned to a state as a prerequisite for the receipt of assistance payments. Social Services Amendments of 1974, Pub.L. No. 93-647, 88 Stat. 2337, 2356 (1975) (codified at 42 U.S.C. § 656(b)). This provision was repealed by the Bankruptcy Reform Act of 1978, Pub.L. No. 95-598, 92 Stat. 2549, 2679. The Bankruptcy Reform Act of 1978 also provided that child support obligations owed directly to the spouse, former spouse, or child of the debtor were *nondischargeable*. 92 Stat. at 2590-91 (codified at 11 U.S.C. § 523(a)(5)(A)). This was the state of the law at the time the five debtors now before us filed their petitions in bankruptcy.

None of the debtors was granted a discharge before Congress reinstituted 42 U.S.C. § 656(b) and amended 11 U.S.C. § 523(a)(5)(A) to again prohibit the discharge of child support obligations assigned to a state as a condition of entitlement to assistance. Omnibus Budget Reconciliation Act of 1981, Pub.L. No. 97-35, 95 Stat. 357, 863. Congress made these provisions effective on enactment (August 13, 1981) rather

than on October 1, 1981, the general date of effectiveness of the Act. 95 Stat. at 863-64. Thus, at the time the judge determined the dischargeability of these child support obligations, the law provided that these debts were not dischargeable.

A.

[2-4] The retroactive application of a federal statute (other than an ex post facto law or a bill of attainder) is not forbidden under the Constitution so long as due process requirements are met.¹ 2 C.D. Sands, *Statutes and Statutory Construction* § 41.03 (4th ed. 1973). Indeed, as a general rule, a judge should apply the law in effect on the date of decision. In *United States v. The Schooner Peggy*, 5 U.S. 103, 1 Cranch 103, 2 L.Ed. 49 (1801), the Supreme Court first set forth the principle in the following language:

It is, in the general, true, that the province of an appellate court is only to inquire whether a judgment, when rendered, was erroneous or not. But if, subsequent to the judgment, and before the decision of the appellate court, a law intervenes and positively changes the rule which governs, the law must be obeyed, or its obligation denied.

5 U.S. at 110, 1 Cranch at 110. In clarifying this rule, in *Thorpe v. Housing Authority of the City of Durham*, 393 U.S. 268, 281-82, 89 S.Ct. 518, 525-26, 21 L.Ed.2d 474 (1969), the Supreme Court ruled that "an appellate court must apply the law in effect at the time it renders its decision," noting

1. In his concurring opinion, Judge Wallace is critical of the majority's discussion of retroactivity. Judge Wallace states: "Admittedly, some have characterized *The Schooner Peggy* as a retroactivity case, see, e.g., Schaefer, *Prospective Rulings: Two Perspectives*, 1982 Sup. Ct.Rev. 1, 19-23, but it is not." (concurring opinion page 1425). Among those authorities which have characterized *The Schooner Peggy* as a "retroactivity case" is the United States Supreme Court. In *Linkletter v. Walker*, 381 U.S. 618, 625, 85 S.Ct. 1731, 1735, 14 L.Ed.2d 601 (1965), the Supreme Court characterized the rule of *The Schooner Peggy* as follows:

"One form of limited retroaction which differs somewhat from the type discussed above

that the *Schooner Peggy* reasoning had been applied whether the change was constitutional, statutory, or judicial. This principle had been applied to a bankruptcy statute in *Carpenter v. Wabash Railway Co.*, 309 U.S. 23, 60 S.Ct. 416, 84 L.Ed. 558 (1940) (amendment to bankruptcy statute enacted while case pending for review held applicable).² We, therefore, must follow the *Schooner Peggy* and apply the law now in effect to the cases before us, unless an exception to the limited retroaction rule is applicable. Legislation is not applied to pending cases where Congress has expressly directed that the law is prospective only or where manifest injustice would result from a retrospective application.

B.

[5] In *Bradley v. School Board of the City of Richmond*, 416 U.S. 696, 94 S.Ct. 2006, 40 L.Ed.2d 476 (1974), the Supreme Court held that "a court is to apply the law in effect at the time it renders its decision, unless . . . there is statutory direction or legislative history to the contrary." *Id.* at 711, 94 S.Ct. at 2016. The Supreme Court also noted in *Bradley* that "even where the intervening law does not explicitly recite that it is to be applied to pending cases, it is to be given recognition and effect." *Id.* at 715, 94 S.Ct. at 2018.

The Omnibus Budget Reconciliation Act of 1981 is silent concerning the application of the statute to pending bankruptcy proceedings. The legislative history is equally barren of any reference to this issue.

is that which was established in *United States v. Schooner Peggy* 1 Cranch 103, 2 L.Ed. 49 (1801).

2. The *Schooner Peggy* reasoning was applied to the same statutory amendment now before us by Judge Shabaz in *re Kuehndorf*, 24 B.R. 555 (W.D.Wis.1982).

A group of decisions in bankruptcy courts have held that a judge must apply the law as of the date of the filing of the petition. See, e.g., *Matter of Flamini*, 19 B.R. 303 (Bkrtcy.E.D. Mich.1982). These decisions ignore the principle that has evolved from the *Schooner Peggy*, which we are compelled to follow.

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The House Conference Report No. 97-208, 97th Cong., 1st Sess., 1986, relating to the Omnibus Budget Reconciliation Act of 1981, simply provides:

Both the House bill and the Senate amendment included the following identical provision which was agreed to by the conferees:

A provision of the Social Security Act, previously in effect, would be reinstated, declaring that a child support obligation assigned to a State as a condition of AFDC eligibility is not discharged in bankruptcy. The provision would be effective upon enactment.

Printed in 1981 U.S.Code Cong. & Ad.News 396, 1348.

While not dispositive on the issue before us, the fact that Congress expressed its intention that the statute take effect upon enactment is some indication that it believed that application of its provisions was urgent. We certainly cannot construe this expression of congressional concern as a direction that the law should *not* be applied to pending matters.

Furthermore, sound public policy and the history of this legislation would support the application of the child support provisions to pending matters.

The obligation of parents to support their children is a matter of paramount social concern. Throughout the history of this child support legislation, parents never were allowed a discharge of a child support obligation owed directly to the other parent or child. For a brief period, however, a parent was allowed to receive a discharge in bankruptcy if the right to receive the support payments had been assigned to the state. As noted above, such an assignment is required by Congress as a condition for a state's participation in the AFDC program. The AFDC program was developed in part to encourage enforcement of the obligation of parents to support their children. S.Rep. No. 93-1356, 93d Cong., 2d Sess., reprinted in 1974 U.S.Code Cong. & Ad.News 8133, 8134, 8145-58. To require a child support obligation to be assigned to a state in order to enforce that obligation and at the same

time to allow a discharge of that obligation because of that very assignment defeats the goal of enforcement of parental duties. This incongruity, plus the fact that Congress made the latest child support amendment effective at an earlier date than the rest of the act (95 Stat. at 863-64), suggests strongly that Congress must have intended that this legislation should be applied to pending cases.

C.

A second exception to the general rule of *Schooner Peggy* arises where application of a change in the law to pending cases would result in manifest injustice. *Thorpe*, 393 U.S. at 282, 89 S.Ct. at 526. Concerns relative to injustice "center upon (a) the nature and identity of the parties, (b) the nature of their rights, and (c) the nature of the impact of the change in law upon those rights." *Bradley*, 416 U.S. at 717, 94 S.Ct. at 2019.

Here, we have on the one hand five fathers who have an obligation to support their children by reason of court decrees ordering a specified amount of support, a common law tradition obligating parents to provide their children with necessities, and a continuing, strong public policy favoring support. On the other hand, we have the State of Idaho, Department of Health and Welfare, a governmental entity charged with the distribution of public funds to the benefit of children who are not receiving support and the responsibility to locate errant parents and to enforce support obligations. It was suggested in the *Schooner Peggy* that a court should not retrospectively affect the rights of private individuals. 5 U.S. at 69. This litigation does not involve "mere private cases between individuals." *Id.* See also *Bradley*, 416 U.S. at 719, 94 S.Ct. at 2020 (school desegregation litigation is a great national concern).

Manifest injustice may also arise from the nature of the rights of the parties. A court would not deprive a party of a right that had matured or become unconditional. *Bradley*, 416 U.S. at 720, 94 S.Ct. at 2020. Furthermore, in matters involving property

rights, retroactive application of a new statute might result in an unconstitutional taking of property without due process of law.

In *Union Pacific Railroad Co. v. Laramie Stock Yards Co.*, 231 U.S. 190, 34 S.Ct. 101, 58 L.Ed. 179 (1913), the Court stated that "the first rule of construction is that legislation must be considered as addressed to the future, not to the past." 231 U.S. at 199, 34 S.Ct. at 102. The *Union Pacific* case involved adverse possession of the railroad's right of way. A retroactive application of the statute, allowing the adverse possession, would have deprived the railroad of its vested property rights; therefore, the Court held that the statute should apply only prospectively. 231 U.S. at 202, 34 S.Ct. at 103.

In *United States v. Security Industrial Bank*, 459 U.S. 70, 103 S.Ct. 407, 411, 74 L.Ed.2d 235 (1982), the Supreme Court found that perfected liens on household furnishings and appliances did involve a property interest of the creditors. A bankruptcy amendment enacted after the liens were perfected allowed debtors to avoid liens on such property. As application of the amendment to perfected liens raised a serious constitutional issue under the fifth amendment, the Court looked to the rules of statutory construction to avoid the constitutional issue. 103 S.Ct. at 412. Relying on *Union Pacific*, the Court held that a statute affecting property rights was meant to be applied only prospectively in the absence of a clear congressional intent that it apply before the enactment date. This construction allowed the Court to avoid the constitutional issue. 103 S.Ct. at 414. In applying this rule of construction, the Court distinguished legislation affecting vested property rights from other laws affecting claims. "This principle has been repeatedly applied to bankruptcy statutes affecting property rights." 103 S.Ct. at 413 (citing *Holt v. Henley*, 232 U.S. 637, 34 S.Ct. 459, 58 L.Ed. 767 (1914) (rights to an automatic sprinkler system); *Auffm'ordt v. Rasin*, 102 U.S. 620, 26 L.Ed. 262 (1881) (rights to certain securities)). The Court noted that in other cases, not involving property rights, new statutes were applied to pend-

ing proceedings: *Claridge Apartments Co. v. Commissioner*, 323 U.S. 141, 65 S.Ct. 172, 89 L.Ed. 139 (1944) (rights to tax benefits); *Dickinson Industrial Site, Inc. v. Cowan*, 309 U.S. 382, 60 S.Ct. 595, 84 L.Ed. 819 (1940) (procedural rules); *Carpenter v. Wabash Railway*, 309 U.S. 23, 60 S.Ct. 416, 84 L.Ed. 558 (1940) (priority of payment of claims); *McFaddin v. Evans-Snyder-Buel Co.*, 185 U.S. 505, 22 S.Ct. 758, 46 L.Ed. 1012 (1902) (curative statute); *Legal Tender Cases*, 79 U.S. 457, 12 Wall. 457, 20 L.Ed. 287 (1870) (payment of debts in legal tender). 103 S.Ct. at 413-414 n. 10.

Under the law in effect at the time of the filing of these bankruptcy petitions, the fathers' assigned child support obligations were dischargeable. The parental duty to pay child support cannot be characterized as a matured or unconditional property right. Until a final decision on dischargeability is made, debtors still are obligated to pay their debts and would be required to do so if the petition were withdrawn. Application of the amendment, disallowing the discharge of these child support obligations, would not deprive the debtors of a matured property right.

The third concern of manifest injustice relates to the nature of the impact of the change in the law upon the rights of the parties. *Bradley* defines this concern as the "possibility that new and unanticipated obligations may be imposed upon a party without notice or an opportunity to be heard." 416 U.S. at 720, 94 S.Ct. at 2021. The 1981 amendment that became effective before any decision was made on the petitions of these debtors did not impose a new obligation on the debtor. Instead, under the amendment parents cannot escape responsibility for an existing obligation. One purpose of the Bankruptcy Reform Act of 1978 was to give debtors a fresh start. That purpose was tempered by other public policies, including enforcement of the parental obligation of support. Thus, the 1978 Act excepted support obligations owed directly to the child or other spouse from discharge. The 1981 amendment reinforces that obligation and allows the states to

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Cite as 726 F.2d 1420 (1984)

carry out their mandate under the AFDC program.

Upon consideration of the parties, the nature of their rights, and the impact of the amendment to 11 U.S.C. § 523(a)(5)(A) upon those rights, we cannot say that application of the amendment to actions pending at the time of the amendment would cause such "manifest injustice" as to compel an exception to the rule that a court applies the law in effect on the date of decision. It is not manifestly unjust to expect parents to meet their responsibilities.

The judgment of the district court is reversed. The debtors' child support obligations were not dischargeable under § 523(a)(5)(A) as amended. The cause is remanded for hearings on the issue of attorney's fees and costs.

WALLACE, Circuit Judge, concurring:

I concur in the result. I write separately to express my view that the majority's discussion of retroactivity is unnecessary and confuses the issue. When the debtors filed their claims, they thought they were entitled to discharge their child support obligations in bankruptcy. This was because their spouses had assigned to Idaho their right to collect those support payments from their husbands. By the time the bankruptcy court rendered its decision, the law had been changed to make those payments non-dischargeable. I believe this case should not be analyzed as one involving the issue of retroactivity, but rather by application of the rule that the courts are governed by the law in effect at the time a decision is rendered, unless it would violate congressional intent or would be manifestly unjust. As the exceptions have not been proven, I would affirm.

The amendment was part of the Omnibus Budget Reconciliation Act of 1981. The Act was largely a fiscal measure designed to reduce federal spending and restore balance to our dual system of government. See 1981 U.S.Cong. & Ad.News, 97th Cong., 1st Sess., p. 396 et seq. States had complained of the economic burdens imposed on them by allowing this type of discharge. See, e.g., *In re Glidden*, 653 F.2d 85, 87 (2d

Cir.1981) (Connecticut's challenge alleged "a possible loss of as much as \$1.25 million in annual payments to the State, as well as a loss of \$47.1 million in accumulated past child support arrearages.").

This case does not involve the abrogation by legislation of established property interests. The debtors had in their favor no court judgments, no liens, and no interests, secured or unsecured, perfected or unperfected. They had no right to prevent removal of the entitlement allowing them to discharge their debts. They only had an expectation that they would be permitted to discharge their child support obligations, along with other debts, in bankruptcy. The debtors' situation differs markedly from the true retroactivity cases the majority cites, e.g., *Holt v. Henley*, 232 U.S. 637, 34 S.Ct. 459, 58 L.Ed. 767 (1914) (effect of bankruptcy amendment on claim of secured creditor who had retained title in bankrupt's personality); *Union Pacific Railroad Co. v. Laramie Stock Yards Co.*, 231 U.S. 190, 34 S.Ct. 101, 58 L.Ed. 179 (1913) (effect of congressional legislation on rights of way granted to railroads by previous act of Congress); *McFaddin v. Evans-Snider-Buel Co.*, 185 U.S. 505, 511-14, 22 S.Ct. 758, 760-61, 20 L.Ed. 287 (1902) (effect of congressional curative act which deprived attaching creditor of property); *Auffm'ordt v. Rasin*, 102 U.S. 620, 26 L.Ed. 262 (1881) (impact of amendatory act on vested rights of bankrupt's assignee to certain wrongly transferred securities).

The majority is correct that this case falls squarely under the rule of *United States v. The Schooner Peggy*, 5 U.S. 103 (1 Cranch), 2 L.Ed. 49 (1801), that an appellate court must apply the law in effect at the time it renders its decision. Admittedly, some have characterized *The Schooner Peggy* as a retroactivity case, see, e.g., Schaefer, *Prospective Rulings: Two Perspectives*, 1982 Sup.Ct.Rev. 1, 19-23, but it is not. The *Peggy* was seized pursuant to a Presidential Commission to capture any armed French vessel found on the high seas. *The Schooner Peggy*, 5 U.S. at 103. Proceedings were begun to condemn the ship and its cargo as prize. *Id.* at 104. The circuit court reversed the district court and found The

Peggy lawful prize. *Id.* at 105-106. While the case was pending before the Supreme Court, the President ratified the Friendship and Commerce Treaty between France and the United States, providing, among other things, for mutual return of "[p]roperty captured, and not yet definitively condemned." The Court stated that "[t]he Constitution of the United States declares a treaty to be supreme law of the land," and that it places an obligation on our courts. *Id.* at 109. No issue of retroactivity of application arose. The Peggy could not be lawful prize.

A case on point followed the clear rule of *The Schooner Peggy*. In *Carpenter v. Wash Ry. Co.*, 309 U.S. 23, 60 S.Ct. 416, 84 L.Ed. 558 (1940), the Court had a case pending when an amendment to the Bankruptcy Act gave railroad employees' personal injuries claims priority not only in bankruptcy, but also in equity receivership cases. 309 U.S. at 26, 60 S.Ct. at 417. As a matter of statutory construction and congressional intent, the Court found the amendment applicable without any discussion of retroactivity. *Id.* at 27-29, 60 S.Ct. at 418-419. The Court was simply "bound . . . to consider and apply the amended statute." *Id.* at 29, 60 S.Ct. 419. It is on this ground that I would affirm.



UNITED STATES of America,
Plaintiff-Appellant,

v.

Samuel Charles GILLYARD,
Defendant-Appellee.

No. 83-5109.

United States Court of Appeals,
Ninth Circuit.

Argued and Submitted Dec. 5, 1983.

Decided Feb. 28, 1984.

Government appealed from order of
the United States District Court for the

Central District of California, David V. Kenyon, J., which suppressed confession. The Court of Appeals, Ferguson, Circuit Judge, held that: (1) there is no per se rule that, once *Miranda* warnings are given prior to a polygraph examination, such warnings need not be given before postexamination accusatory questioning, and (2) evidence sustained determination that defendant had not properly waived *Miranda* rights.

Affirmed.

1. Criminal Law ⇐412.2(2)

Fifth Amendment right to counsel first arises when an individual is held for custodial interrogation; suspect is in custody and entitled to *Miranda* warnings if, under the circumstances, a reasonable person would believe that he is not free to leave. U.S.C.A. Const.Amend. 5.

2. Criminal Law ⇐1158(4)

District court finding that defendant was in custody and entitled to *Miranda* warnings will be upheld unless it is clearly erroneous.

3. Criminal Law ⇐414

Evidence sustained finding that defendant who had been given *Miranda* rights prior to taking polygraph examination but who was not given *Miranda* rights when he was thereafter interrogated by the polygraph operator and then by postal inspectors had not properly waived his rights.

4. Criminal Law ⇐412.2(3)

There is no per se rule that, once *Miranda* warnings are given prior to a polygraph examination, the warnings need not be given before postexamination accusatory questioning.

Duane Deskins, Asst. U.S. Atty., Los Angeles, Cal., for plaintiff-appellant.

Randy Sue Pollock, Deputy Federal Public Defender, Los Angeles, Cal., for defendant-appellee.

Senator HEFLIN. I will ask you the same question I asked Senator Rudman. Assuming that a utility fails to get a fair and reasonable rate of return, and the utility appeals to the Supreme Court and loses the appeal. After several years the utility becomes insolvent and files bankruptcy. Can the bankruptcy court, under present law, in effect increase rates either directly or indirectly in order to provide additional revenues under a plan of reorganization?

Do you think, excluding all things about Seabrook and bondholders and anything else, just the hypothetical case of whether or not a utility becomes insolvent as a result of inadequate rates, does the bankruptcy court in a plan of reorganization have the authority under existing law to raise the rates?

Mr. SMUCKLER. Senator, Larry Smuckler. We believe that the bankruptcy court does not have the authority to raise rates itself. Section 1129 of the Bankruptcy Code does require that rates be approved by the appropriate regulatory authority. And I think as Senator Rudman stated, the maneuver here by Public Service Co. of New Hampshire is a maneuver to evade that requirement by changing the State regulatory authority. But in either event, changes in rates under section 1129(a)(6) of the code have to be approved by a regulatory authority and not by the judge.

Mr. VAUGHN. May I clarify that to some degree? My name is Mark Vaughn. I happen to be one of the bankruptcy lawyers for the State.

Senator HEFLIN. Yes, sir.

Mr. VAUGHN. Under current law, section 959(b) of title 28 U.S.C. clearly states that a trustee as a debtor in possession during a course of the bankruptcy has to comply with State law. I do not think there is any question that rates during the pendency of a chapter 11 proceeding have to comply with the State law. I do not think there is any question about that.

The question is can they use the plan of reorganization in the confirmation proceedings to get around with that. There is some case law saying that 28 U.S.C. 959(b) does not apply in the confirmation proceedings. It is our position that section 1123, which is the provision of the Bankruptcy Code entitled "Contents of a Plan," that is the provision that Public Service in the instant case is using to say that they can disregard State regulatory law in the confirmation process in the plan process.

I would like the Senators to—the predecessor to 1123(a) was section 216 of the Bankruptcy Act. Nowhere does the opponents mention section 216, but that was the predecessor to 1123. And clearly under—I think it is clear under the predecessor, under chapter 10, that the general consensus was that planned proponents on the confirmation process had to comply with State law, and I would cite Collier's, volume 6, section 1019, which basically says whenever the mean is chosen it must be remembered that conformity with other applicable State or Federal laws may be necessary, and the plan should be drawn with that in mind.

Now when 1123 came about in 1978, there was no legislative history with respect to changing that, and in 1984 the language under the rubric of technical amendments was added, notwithstanding any other applicable nonbankruptcy law was added. And under the rubric of a technical amendment, and in that language alone is

where they are seeking the power to really upset the matter of federalism which is really the issue here.

And I think to answer Senator Grassley's earlier question as to why this is different than the usual case, having to do with the pending case, is No. 1 it really is a clarification. It really does not change the law, and two, the second issue is federalism and that takes it out of the run of the mill cases.

Senator HEFLIN. Under section 1129, title 28, it reads the court shall confirm a plan only if all of the following requirements are met. Then it lists the requirements. Under 6 it says "any governmental regulatory commission with jurisdiction, after confirmation of the plan, over the rates of the debtor has approved any rate change provided for in the plan, or such rate change is especially conditioned on such approval." It says governmental regulatory commission. I suppose that means Federal and State and the commission would, I would assume, be plural. What is your explanation of section 1129(b)?

Mr. VAUGHN. I think the answer, Senator, is that under State law, as it exists today, in order to change from regulation from New Hampshire PUC to Federal regulation under FERC, they would have to get approval of certain matters from the New Hampshire Public Utilities Commission. That is what they are trying to avoid by using the plan of reorganization. The section 1129 talks about the regulatory agency having jurisdiction after the confirmation, and what they are saying in this case, that is the FERC and no longer the New Hampshire regulatory agency. And that is exactly the point that we are here for today.

Senator HEFLIN. All right, sir. Senator Grassley.

Senator GRASSLEY. On that point, the first sentence of that subsection says the court shall confirm a plan only if, only if, all the following requirements are met, and one of those requirements are:

(6) any government regulatory commission with jurisdiction after confirmation of the plan over the rates the debtor has approved, any rate change provided for in the plan and such rate change is especially conditioned on such approval.

Mr. VAUGHN. I will let Mr. Smuckler. He is more of a utility lawyer. He can give you the details of what is being done here.

Mr. SMUCKLER. Senator, the language in that section says the regulatory commission with authority over rates has to approve the rates. In order to implement therefore a plan, Public Service Co. in this instance has to disaggregate its functions, its generation and transmission function into one company, its distribution function into another company in order to create sort of a paper fiction that they are engaging in first a wholesale transaction and then reselling that to the public. And it is that wholesale transaction that, in fact, causes it to be subject to the regulation of the Federal Energy Regulatory Commission.

That disaggregation may or may not be proper. That is not the issue. The issue is that in normal circumstances, that disaggregation including approvals of financings, transfers of assets, the granting of new franchises, is subject to the jurisdiction of the New Hampshire Public Utilities Commission, and it is precisely those quote "nonrate" functions that they are seeking to preempt.

And once they have gotten the bankruptcy court to do that, they will have, in effect, removed the ratemaking jurisdiction from the New Hampshire Commission and federalized it in the FERC.

Senator GRASSLEY. So you are taking the position that this section does not protect the ratepayers in New Hampshire regardless of what stand FERC takes on the cost of construction aspects of it.

Mr. SMUCKLER. If Public Service Co. is successful in claiming that it can preempt those quote "nonrate" areas of regulation, if they can preempt the State's authority to approve the purchase power contract between the wholesaler and the retailer, which they are seeking to do so that the PUC cannot even review the prudence of entering into a high cost wholesale contract, then as Senator Rudman testified the state PUC has no authority but to flow through the wholesale rates approved by the FERC.

It will have the authority over the retail rates, but if total rates are in the area of 10 cents and wholesale rates are 8 cents of it, it is very little authority indeed.

Senator GRASSLEY. And are you saying the bankruptcy law is so specific that they will not be able to circumvent the Public Utility Commission of New Hampshire.

Mr. SMUCKLER. Public Service Co. is certainly claiming they can do that. We do not believe they can, and that is why we are seeking the clarification with the Congress today.

Senator HEFLIN. Senator Grassley. You have another question?

Senator GRASSLEY. Yes, if I could, please. The negotiations regarding the reorganization are going on between the company, the State of New Hampshire, and representatives of the creditors and the stockholders. This bill, if enacted, would dramatically affect those negotiations, and so I need to know from you folks why you think Congress should take these extraordinary steps of short-circuiting good-faith negotiations?

Mr. SMUCKLER. Senator, I guess I would make two points. One is, as Public Service Co. itself eloquently argued before the bankruptcy court, decisions should not be postponed because of the possibility of a settlement. The matter has to go on. But more importantly than that, I think that this is not just a New Hampshire problem. If the law is or can be interpreted because of an ambiguity as allowing utilities that are dissatisfied with the decisions of their State regulators to evade that regulation by going to bankruptcy court, particularly given that insolvency is no longer a requirement for seeking chapter 11, this is a nationwide problem, and it is something that we would respectfully request Congress to address.

Senator GRASSLEY. As I understand it, the bill would require that the State give its prior approval before any reorganization plan will be confirmed, and so inasmuch as the State of New Hampshire is already a full party to the bankruptcy and can probably effectively block a plan, why is the bill not redundant?

Mr. VAUGHN. No. 1, on the bankruptcy issue there is no indication that the State of New Hampshire can block a plan. The State of New Hampshire over the violent objection of the creditors and of the Public Service Co. has been admitted as a party and interest and the information from the Public Service Co. would think that now the bankruptcy judge as the final arbiter is going to protect the interest of the ratepayer.

The ratepayers are the one constituency in the chapter 11 proceeding that do not vote. The creditors vote. The equity probably will vote, but the ratepayers do not vote. And so the final decision on a plan is not in the hands of the State. It is in the hands of the creditors.

Senator GRASSLEY. Does not the State of New Hampshire vote as a party?

Mr. VAUGHN. No, it does not. The State of New Hampshire is a creditor of some amount, but as a party it has no unique—

Senator GRASSLEY. No vote.

Mr. VAUGHN. No vote. And I would like to also point out, Your Honor, or Senator, that one of the differences between the provisions of chapter 11 and the provisions of chapter 11 having to do with railroad reorganization is that the railroad reorganization provisions tell the court that it has to in making these decisions on confirmation has to take the public interest into effect.

There is no such provision for an ordinary chapter 11, and there is no such provision for a utility chapter 11.

Senator GRASSLEY. I am sure you are making the same arguments in court as you are making here today. Do you not think that the court is going to be a fair arbiter?

Mr. VAUGHN. I am not sure I want to answer that since the matter is still before the courts.

Senator GRASSLEY. I am not sure you have to answer, but you are making arguments here today, and you made those same arguments in court.

Mr. VAUGHN. It is a matter of federalism that are very important to the State of New Hampshire, and as Mr. Smuckler said, we think the matter has to go forward.

Mr. SMUCKLER. Senator, if I can add one other thing. The State is not, contrary to what has been argued, seeking to exercise an effective veto over this thing. The legislation as we understand it simply leaves intact the current state regulatory process. Now that process does not address things that are particularly within the province of the bankruptcy court and with what we do not contend we should have veto power, things like how revenues or value are to be distributed, for example, among the various creditor classes.

That is something that is between the debtor and its creditors and is in the province of the bankruptcy court and is not something that normal regulation pertains to, nor are we seeking to expand the role of normal regulation to pertain to those type of issues.

Senator GRASSLEY. Somewhere along the line the statement was made, and I would be more convinced about that statement that this bill is more than about the New Hampshire situation if you would agree to strike that provision that making S. 46 applicable to pending cases. Are you willing to do that?

Mr. VAUGHN. Your Honor, I—

Senator GRASSLEY. Well, the point is you are saying that this legislation is important, about more than just the New Hampshire case. And we in most every case I know of, in fact, I guess every case I know of, legislation along this line has been prospective, not affecting pending cases. And so I am asking you about if this is

about more than just the New Hampshire case, about your view of striking the applicability to pending cases.

Mr. STAHL. Senator, if that happened, I suppose the bankruptcy judge would take note of the fact that the Senate and the House had taken a stand in passing the clarification. It would seem unfortunate and unfair not to apply the statute to the facts which exist, and I suppose it can be done. I suppose the judge would take some notice if he had not already made his decision or some appellate court would perhaps take notice of the fact of what the Congress had done in clarifying the act.

Senator GRASSLEY. Well, are there any other pending cases that you know about that are affected by this legislation?

Mr. STAHL. Not at the moment, but I would expect that there are other utilities. We know of other utilities which have had problems because of nuclear installations who might very well want to take the same route in order to get around anti-CWIP statutes if they existed in their jurisdictions.

Senator GRASSLEY. Do you know of any other case since the 1978 enactment where the code was amended in a way that applied to pending cases? Probably not?

Mr. VAUGHN. No. I would cite the case of the matter of Eugene L. Reynolds. It is a ninth circuit case, which is 726 F.2d 1420. That had to do with the modification of the Bankruptcy Code having to do with support payments to spouses. It was an Idaho case. The ninth circuit in that case found basically that the general rule is that a court applies the law at the time it makes its decision, and unless there is some unfair taking, there is no constitutional reason why a law passed while a matter was pending does not affect. In fact, the general rule is that the court has to look at the law as it stands when it makes its decision.

That had to do with support payments being assigned to the State of Idaho, and for a short period of time debtors were being granted dischargeability in an otherwise nondischargeable situation because the language of the Bankruptcy Code said only if the obligation was to the spouse or the children, and it neglected to say it could be assigned to the State. I am not sure that is exactly on point, Senator Grassley, but I think it surely is a case that stands for the proposition if there is no constitutional limitation in modifying law and having it affect pending cases.

Senator GRASSLEY. Do you favor a reorganized and revitalized New Hampshire Public Service Co., and if so, how have you demonstrated that to the court?

Mr. SMUCKLER. I think, Senator, the short answer to your question is yes. It is to the benefit of the State and its ratepayers to have a financially strong utility that has the ability to meet New Hampshire's critical electrical energy and capacity needs in the coming years, has access to the financial markets, and can do so at rates that are just and reasonable. And we have done that by participating in the bankruptcy court seeking to ensure that State legal requirements are adhered to and seeking through the negotiating process in facilitating a consensual plan that best balances all interests in this case given the risk, the allocation of risks and benefits that have occurred to date.

Senator GRASSLEY. Mr. Chairman, I am finished.

Senator HEFLIN. Senator Thurmond.

Senator THURMOND. Thank you. I will ask the questions here of Mr. Arnold, but any of you can answer them who wish to. Mr. Arnold, in your opinion, what is fundamentally unique about the reorganization of an electric utility company that would warrant the special treatment afforded by S. 46?

Mr. SMUCKLER. Senator, Larry Smuckler. The unique nature of this is that the electric utility is a franchise monopoly. It is allowed to operate as a monopoly with customers who do not have a choice as they would with other products of purchasing from company A or company B. They have to purchase from the electric utility that the State has said has the exclusive right to provide them with power.

Now generally that kind of monopoly is a violation of the anti-trust laws, but under *Parker versus Brown*, the court held that where there is a comprehensive system of State regulation, it is not a violation of the antitrust laws. In this instance, what the ambiguity that Public Service Co. is seeking to take advantage of will allow it to operate as it wishes without being subject to the normal regulatory laws that control monopoly abuse.

And I think that that is a fundamental difference between this and nonmonopoly kinds of bankruptcies where, if you will, in a nonmonopoly bankruptcy the market is a constraint that says that the cost cannot go up a certain amount, and the pie is only so big, and that is what has to be divided up between the various customer classes.

With a regulated monopoly, instead of a competitive market setting that particular size of the pie, it is the regulatory agency, and all we are saying is that the regulatory agency should be able to continue to perform its function of balancing investor and ratepayer interest to make sure that there is no monopoly abuse.

Senator THURMOND. Mr. Arnold, chapter 11 of the Bankruptcy Code is designed to reorganize corporations to avoid liquidation, to pay creditors, and to allow the business to continue in operation. Energy regulation and rate setting for utilities appears outside the scope of the Bankruptcy Code's jurisdiction. If the policies of the Federal Energy Regulatory Commission are objectionable, or the two-tier regulatory structure insufficient to protect consumers, would it not be better to introduce legislation concerning these broader issues rather than to amend the Bankruptcy Code regarding this specific case?

Mr. SMUCKLER. Senator, I think that our reading of the Bankruptcy Code, and if S. 46 is passed, it would be clarified to make it explicit, is that it may be appropriate under some circumstances for a company to become federally regulated, but they have to go through the requirements of the State regulatory process to get there.

We think that the code now requires that, but an ambiguity has been exploited, and we think that it ought to be clarified so that it is no longer ambiguous, and it is clear that they are required to continue to adhere to those State regulatory requirements. If they do that, there is no imbalance in the Federal energy laws or the jurisdiction of the Federal Energy Regulatory Commission that Congress need address on this issue in our judgment.

Senator THURMOND. Has any thought be given to legislation that would prohibit the Federal Energy Regulatory Commission from fixing rates in the State?

Mr. SMUCKLER. We think that the proposed legislation, we have not given that thought because the proposed legislation, as I have said, is clarifying legislation about what a debtor or a bankrupt debtor utility can do under the Bankruptcy Code. In the absence of that Bankruptcy Code, a loophole, if you will, or at least the loophole claimed by Public Service, we think that the system works quite well.

It is the disturbance of the existing Federal/State balance under the energy laws introduced by their interpretation of the Bankruptcy Code that needs to be addressed, not the balance of, not the Federal energy laws itself.

Senator THURMOND. You do not think it is worthy of consideration to consider a bill to prohibit the Federal Energy Regulation Commission from fixing the State rates?

Mr. SMUCKLER. It may be. It may very well be to address other nonbankruptcy problems.

Senator THURMOND. Would that accomplish your purpose?

Mr. SMUCKLER. Yes, it would.

Senator THURMOND. Would that accomplish your purpose?

Mr. SMUCKLER. Yes. But that would be broader than what we believe is needed for this particular problem.

Mr. STAHL. Senator, there is one other issue here. Part of this reorganization plan requires the power contract to be approved by FERC, and once that power contract is approved, as we have pointed out in our earlier testimony, the State agency would have no way of dealing with that.

In other words, if cheaper power became available, normally the State agency could say to the retail company buy that. But with this plan, again, that would not be possible. That fixed rate power contract if approved, it is the company's position would flow through and the State regulatory agency would have an illusory right to do something about it.

Mr. SMUCKLER. One additional point, Senator. A change in the Federal Energy Regulatory laws rather than the Bankruptcy Code might be construed more in the nature of a change in the law rather than a clarification, and as we have pointed out, we believe that we are seeking a clarification of the existing Bankruptcy Code.

Senator THURMOND. Retroactive legislation has traditionally been viewed as objectionable because it deprives citizens of the ability to plan their conduct with reasonable certainty of legal consequences. You understand that?

Mr. STAHL. Yes, Senator.

Senator THURMOND. In other words, generally speaking retroactive legislation has traditionally been viewed as objectionable because citizens cannot plan their future. Now, if S. 46 is enacted, it would apply to Public Service Co. of New Hampshire's reorganization currently before the bankruptcy court. I believe, in this case, is it your opinion that State regulation of utility rates outweighs the need for uniformity and predictability of our laws?

Mr. STAHL. Well, I would think, Senator, that the consumer who ultimately is the party who is going to have to pay for this should

be and have the right to be considered in this process. And by this clarification, all that we do is we leave to the State regulatory agency what was already there: the determination of a just and reasonable rate that the ratepayer should pay and the company should receive.

So it really is not changing what this company believed it had. Remember back in 1978 before it began to make its massive investments in the Seabrook nuclear plant, it knew what the regulatory scheme was. New Hampshire had clearly adapted and adopted the anti-CWIP legislation. This company and its stockholders which permitted its management to remain in place recognized what the scheme was.

Now what is seeks to do is to say, well, we made a mistake, and we really want to pay back all those people who knew what the risk was, and we want to pay it back at the expense of the people who said upfront if you do this, you do it at certain risk. You will only know when it is all over, the process is over, what portion of your investment will have been found to be prudent and used and useful and go ultimately into rate base.

The people who are being affected by this change really are the ratepayers because the ratepayers understood and they told the company, a private company, with a monopoly customer base what to expect in regulation so I do not think that this clarification is unfair to the investor or to the bondholder.

Senator THURMOND. Now when a company goes into bankruptcy, it means that the income is not sufficient to operate; is that your understanding?

Mr. STAHL. This company had sufficient income to operate. It has always been——

Senator THURMOND. And pay its debts.

Mr. STAHL [continuing]. A successful company. What it did was it made an investment in Seabrook which ran over any of its expectations, borrowed money at very heavy rates of interest and found that it could not pay those people back, and that is what put it back, put it into bankruptcy.

Senator THURMOND. Well, when a company goes in bankruptcy, they have got to do one of two things, have they not? Either raise more income or reduce expenditures.

Mr. STAHL. That is correct, Senator, except if you assume that the raising of more income should be done at the expense of a monopoly customer base. If you were selling automobiles, you could not raise the rate of the automobile in order to pay off your investors who had made an imprudent investment because elasticity in the market would not permit that. And I would venture to say that that is the same issue here.

Senator THURMOND. Well, now take this company or any company. If their expenses are more than income to operate, they go in bankruptcy. Well, then that means they either have to raise more money in some way or they must cut expenses or they cannot survive; is that correct?

Mr. STAHL. Well, I think in a regulated utility, it is a little bit different. In a normal industrial bankruptcy, that is correct. You have to cut your expenses, and you have to have your products sell

and raise more income so that you are able to meet your newly re-organized needs.

Senator THURMOND. Now if this bill is not passed, they would be allowed to increase rates some, would they not?

Mr. STAHL. Well, they will be allowed to increase rates probably under any scenario. The only question is how much that increase is going to be.

Senator THURMOND. Well, I would like to ask this. If this bill does pass, would the utility commission that regulates rates in New Hampshire allow them to raise enough to survive?

Mr. SMUCKLER. Senator, New Hampshire public utility law explicitly provides that the commission has to balance the interest of companies and ratepayers. It cannot consider one interest without balancing the other.

Senator THURMOND. Well, in other words, then, if this bill passes, the regulatory commission in New Hampshire that controls the rates could take steps necessary to allow the company to survive?

Mr. SMUCKLER. That is correct, Senator.

Senator THURMOND. And as I construe it, that is the law and they would have to do it; is that right?

Mr. SMUCKLER. That is right. All we are asking for is that the State regulatory commission continue to be able to exercise the same functions that it has always exercised.

Mr. VAUGHN. May I just answer, Senator.

Senator HEFLIN. We are going to have to move along. We can have one person respond because we have another hearing that was scheduled at 11:30.

Senator THURMOND. Mr. Chairman, I am about through anyway.

Senator HEFLIN. All right. Rather than having everybody comment on the same question, go ahead, sir. You have another question.

Senator THURMOND. That is all right. I just wanted to know that if this bill does pass, is there some way that this Seabrook company can survive, and I believe his answer was the utility commission that regulates rates in New Hampshire would have the power to grant such relief as necessary to enable them to survive, and the law even required them to do that?

Mr. SMUCKLER. The law requires them to consider investor interests as well as ratepayer interests and within constitutional requirements that prohibits the commission from depriving investors of their property without due process. They would have to comply with those requirements.

Senator THURMOND. That is all, Mr. Chairman. Thank you.

Senator HEFLIN. Thank you. We appreciate it.

Senator HEFLIN. The next witness is Mr. Richard Levin of Los Angeles. Come forward, Mr. Levin. I would ask you to summarize your statement. Your full statement will be made a part of the record.

STATEMENT OF RICHARD LEVIN, STUTMAN, TREISTER & GLATT,
LOS ANGELES, CA

Mr. LEVIN. Yes, I had intended to, Mr. Chairman. Thank you and thank you for the invitation to return once again to this subcom-

mittee. It is always a pleasure to assist in the formulation of the bankruptcy laws, and I do appreciate the opportunity. As you know, I not only have served the other body as a staff member when the 1978 Bankruptcy Code was written, but I have an extra perspective on this case as I am the corporate reorganization counsel for Public Service Co. of New Hampshire.

There are three points I would like to make this morning, Mr. Chairman. First, S. 46 is not likely to solve any rate issue in New Hampshire or to protect consumers. Second, S. 46 is not good bankruptcy law. And third, making S. 46 retroactive is both unfair and unwise, and I will address each of those very briefly if I may.

You have heard proponents of S. 46 claim that it is necessary to prevent Public Service from using the bankruptcy law to evade the New Hampshire anti-CWIP law at a time now when Seabrook operation or at a time then, a year ago, when Seabrook's operation was uncertain. Seabrook's operation now seems assured—even its opponents have so admitted—that it is merely a question of time. And the anti-CWIP law that the prior witnesses have been concerned about would no longer be an impediment to the New Hampshire Public Utility Commission granting just and reasonable rates, balancing the interest of customers and investors. So this bill is not needed and should not be used to settle a local dispute over rates.

Second, the 1978 Bankruptcy Code balanced many factors in setting the reorganization chapter. One of those factors was the role of regulatory agencies in bankruptcy cases. My prepared statement traces that decision in the code and its legislative history in detail, and I will not repeat it.

What is important is the policy behind that decision, and that policy is still sound. That is that the bankruptcy court is the neutral forum. It protects all interests in the case as Judge Whelan has noted in his prepared statement this morning. It protects creditors, the debtor, the public interest, and all you have to do is pick up any volume of the bankruptcy reports and see the discussion of the public interest, not only in utility cases but all bankruptcy cases.

That is especially so here that the bankruptcy court is the neutral forum where the bankruptcy judge has explicitly recognized the standing of the State of New Hampshire for all purposes in the case. And it has recognized the standing of several other parties such as the consumer advocate and the business and industry affairs council for issues related to rates, for any hearing on issues related to rates.

To allow one party to a bankruptcy case such as the State of New Hampshire in this Public Service case to make many of the decisions affecting the reorganization as S. 46 would do is to undo totally the careful compromises that were crafted in 1978, and it would give the State agencies far more authority than even Federal agencies such as the ICC were granted in railroad cases.

No one suggests that the bankruptcy court should be setting rates although Mr. Vaughn so testified in 1984 before the New Hampshire PUC. But by the same token the public utility commissions of any States should not be reorganizing debtors. That is the province of the bankruptcy court, and that should not be invaded.

If any bankruptcy law is appropriate at all, it is to recognize explicitly the standing of the State authorities as the bankruptcy judge has done already in this case.

And third, I want to talk about retroactivity, which is both unfair and unwise. Keep in mind that the question we have here is under submission now at the bankruptcy court. It has been briefed and argued and a decision is expected soon. No one would suggest in any other context that changing the rules in the middle of the game is unfair, and if the proponents of this legislation is correct, that this simply clarifies existing law, then there is no need to make it applicable to existing law. It already applies.

And if they are incorrect, then it is changing the rules. There argument is somewhat disingenuous. It is clearly within Congress' power to make it retroactive. I do not dispute that, but that is a dirty business, and absent some compelling national interest, which is not present here to make it retroactive, it should not be done.

Prospective legislation would adequately address the concern about a flood of cases in the bankruptcy court to utilize the law as it now exists. And it is unwise to make it retroactive. This bill is an open invitation to litigate every bankruptcy case with political interest here instead of in the bankruptcy court, as we have already seen this morning. The mere fact that I am here and the predecessor witnesses are here, we were the litigants before the bankruptcy court a month ago, and here we are again.

This committee should not set a precedent of inviting parties to bankruptcy cases to work out their differences here. The bankruptcy process was designed to accommodate a consensual plan. It is working in this case, and Congress should stand by its decision in 1978 to permit that process to go forward.

Senator HEFLIN. If you will summarize in about a minute.

Mr. LEVIN. That completes my statement, Mr. Chairman. Thank you.

[The statement of Mr. Levin and responses to followup questions submitted by Senators Heflin, Grassley, and Thurmond follow:]

Statement
of
Richard B. Levin, Esq.
Stutman, Treister & Glatt

Before the
Senate Judiciary Subcommittee
on
Courts and Administrative Practice
Regarding S.46

July 26, 1989

STATEMENT OF RICHARD B. LEVIN

Mr. Chairman, and Members of the Subcommittee:

My name is Richard B. Levin. I very much appreciate this opportunity to address the Subcommittee with respect to S.46, the "Electric Utilities Bankruptcy Clarification Act." I am a partner in the law firm of Stutman, Treister and Glatt, where I specialize in bankruptcy, insolvency, and corporate reorganization law. Indeed, all of my professional life as a lawyer has focused on bankruptcy law. From 1975 to 1978, I served as Counsel to the House Judiciary Subcommittee on Civil and Constitutional Rights, chaired by Congressman Don Edwards. As you will recall, at that time that Subcommittee was your counterpart in the other body, working on what became the Bankruptcy Reform Act of 1978. So I have had the opportunity to participate in the creation of our modern system of bankruptcy law and to spend the last decade actually working within that system. Over that time I have continued to write on a number of subjects pertaining to bankruptcy law and presently serve as a Consulting Editor and Contributing Editor for Collier on Bankruptcy. I have also been very active in the National Bankruptcy Conference, and have testified in the past before this Subcommittee on behalf of the Conference. My testimony today, however, is not on behalf of the Conference, which is represented here today by its Chairman, Leonard Rosen.

Instead, I currently represent Public Service Company of New Hampshire in its Chapter 11 case, which has given rise to the bill that is the subject of today's hearing, and I am testifying on its behalf. From this perspective, I am able to offer you not only my general knowledge and expertise on bankruptcy law, but also my specific knowledge of how the Code has worked in the particular case of the bankruptcy of Public Service.

INTRODUCTION

If I could leave you with only one thought as a result of today's hearing, it would be this: Congress worked long and hard in the thorough overhaul of an outmoded bankruptcy system in 1978. You did an exceptional job in fashioning a modern bankruptcy system that effectively and fairly balances and responds to the needs of all those interested in a reorganizing company.

The success of the 1978 effort is no more clearly seen than in the revised procedures governing corporate reorganization and rehabilitation. In Chapter 11 of the Code many procedures and layers of bureaucratic review were streamlined into a single process dominated by one neutral arbiter -- the bankruptcy court. Unlike any other regulatory agency -- state or federal -- that had a significant role in the reorganization process under the old law, the mission of the bankruptcy court in Chapter 11 proceedings is solely devoted to undertaking an impartial

balancing of all the public and private interests implicated in the effort to put a bankrupt company back on its feet.

S.46 comes onto the scene as a hastily and ill-conceived, unnecessary piece of legislation that truly proposes to "turn back the clock" in bankruptcy practice. This bill would change the law to require the approval of non-bankruptcy regulators, who would have had jurisdiction outside of the bankruptcy context, before the bankruptcy court can confirm a plan of reorganization. By so doing, it once again interjects into the process the non-bankruptcy bureaucratic control over corporate reorganization that Congress in 1978 labored so hard to eliminate. This vice is compounded by the fact that S.46 is explicitly made applicable to pending bankruptcy cases, a palpably unfair feature of this bill regardless of its substantive merits.

Of course, the reason that this bill is explicitly applicable to pending cases is that S.46 is really not driven by a substantive bankruptcy concern, but by a parochial desire to block a possible result in a particular bankruptcy proceeding -- that of Public Service Company of New Hampshire. To be sure, the temptation to use a body of law as a pawn in a particular case is strong in bankruptcy, where a variety of interested parties -- some with considerable political muscle -- are contending over the future, or the remains, of a failing company in which they have considerable financial interest. For

that reason, in the area of bankruptcy legislation Congress has historically taken great pains to avoid making changes in the law applicable to pending cases. Even if one were persuaded of the merits of S.46 -- which I am not -- there is no reason to make this legislation applicable to pending cases.

**S.46 IS INCONSISTENT WITH THE DESIGN
OF THE BANKRUPTCY CODE OF 1978**

The Bankruptcy Code reflects a conscious attempt by Congress to reduce non-bankruptcy regulatory control over reorganization plans and make the bankruptcy court the focal point for plan confirmation. Examination of the change in the law crafted by Congress in 1978, and of the legislative history underlying that change, clearly demonstrates that S.46, far from "clarifying" some ambiguity in the Code as its sponsors suggest, would make a substantial change in the law that is fundamentally at odds with the design of the 1978 Code.

The Revision of the Law in 1978

In enacting the Bankruptcy Code and repealing the former Bankruptcy Act, Congress dramatically scaled back the broad role that both state and federal regulatory commissions had previously played in the reorganization of utilities under the federal bankruptcy laws. Indeed, it repealed the veto power that S.46 now seeks to recreate.

Unlike the current Bankruptcy Code, Chapter X of the former Bankruptcy Act required that the governing state regulatory commission have an opportunity to comment on a plan involving the reorganization of a public utility:

In case a debtor is a public-utility corporation, subject to the jurisdiction of a commission having regulatory jurisdiction over the debtor, a plan shall not be approved, as provided in section 174 of this Act, until--

(1) it shall have been submitted to each such commission;

(2) an opportunity shall have been afforded each such commission to suggest amendments or offer objections to the plan; and

(3) the judge shall have considered such amendments or objections at a hearing at which such commission may be heard.

Bankruptcy Act § 177, former 11 U.S.C. § 577. No similar provision appears in the Bankruptcy Code.

Much more importantly, the former Bankruptcy Act specifically made a plan of reorganization for an intrastate public utility subject to the approval of the governing state regulatory commission:

In case a debtor is a public utility corporation, wholly intrastate, subject to the jurisdiction of a State commission having regulatory jurisdiction over such debtor, a plan shall not be approved, as provided in section 174 of this Act, unless such State commission shall have first certified its approval of such plan as to the public interest therein and the fairness thereof.

Upon its failure to certify its approval or disapproval within thirty days, or such further time as the court may may prescribe, after the submission of the plan to it, as provided in section 177 of this Act, the public interest shall, for the purposes of such approval and of the confirmation of the plan, not be deemed to be affected by the plan. (emphasis added).

Bankruptcy Act § 178, former 11 U.S.C. § 578. No similar provision appears in the Bankruptcy Code.

Moreover, former Chapter X specifically required that a public utility undergoing reorganization obtain the approval of the governing regulatory agency before implementing a confirmed plan:

Upon confirmation of a plan--

. . . .

(2) the debtor and every other corporation organized or to be organized for the purpose of carrying out the plan shall comply with the provisions of the plan and with all orders of the court relative thereto and shall take all action necessary to carry out the plan, including, in the case of a public-utility corporation, the procuring of authorization, approval, or consent of each commission having regulatory jurisdiction over the debtor or such other corporation .

. . . .

Bankruptcy Act § 224(2), former 11 U.S.C. § 624(2) (emphasis added). The emphasized language was not carried over into the Bankruptcy Code.

Thus, had Congress sought to subject the provisions of a plan for a public utility to non-bankruptcy regulatory approval when it enacted the Bankruptcy Code, it had a model for doing so

in the provisions of former Chapter X. Congress did not, however, follow that model. Instead, in contrast to the broad and pervasive requirements of prior regulatory review and approval of a reorganization plan for a public utility that governed under former Chapter X, the Bankruptcy Code now contains a narrow requirement of regulatory approval which applies only to a rate change provided in a plan. Section 1129(a)(6) of the Code, 11 U.S.C. § 1129(a)(6), provides that in order for a plan to be confirmed,

any governmental regulatory commission with jurisdiction, after confirmation of the plan, over the rates of the debtor has approved any rate change provided for in the plan, or such rate change is expressly conditioned on such approval.

Unlike its statutory predecessor, the Bankruptcy Code subjects no other element of a Chapter 11 plan for a public utility to regulatory review or approval. Section 1129(a)(6) does not cover any other actions which are within the jurisdiction of the PUC or require regulatory approval therefor. Moreover, the Bankruptcy Code counterpart to section 224(2) of the former Bankruptcy Act, present 11 U.S.C. § 1142(a), contains no requirement like that in former section 224(2), requiring that a public utility undergoing reorganization obtain regulatory approval prior to implementing a confirmed Chapter 11 plan.

Of course, Congress' effort to streamline the reorganization process was not aimed only at state non-bankruptcy regulatory

agencies. The role of federal regulatory authorities was also greatly reduced.

Under prior law, the Interstate Commerce Commission ("ICC") totally dominated the plan approval process in a railroad reorganization: "No plan shall be approved or confirmed by the judge in any proceeding under this section unless the plan shall first have been approved by the Commission and certified to the court." Bankruptcy Act section 77(d), 11 U.S.C. § 22205(d) (repealed). In addition, the Bankruptcy Act allowed burdensome and unprofitable rail lines to be abandoned "only with the approval and authorization of the Commission when required by the Interstate Commerce Act." Bankruptcy Act section 77(o), 11 U.S.C. § 205(o) (repealed)).

Congress dramatically reduced the power of the ICC in railroad reorganization proceedings when it enacted the Code. A plan no longer need be submitted to the ICC for approval before confirmation. Section 1173 of the Code, which sets forth the conditions to confirmation of a plan for a railroad, includes no requirement of ICC approval; indeed, it does not even mention the ICC. In fact, the ICC is given no special power regarding plan confirmation or plan formulation. Instead, it is now the bankruptcy court, rather than the ICC, which makes public interest determinations. 5 Collier on Bankruptcy, ¶ 1173.03, at 1173-6 (15th ed. 1988); see 11 U.S.C. § 1165.

Although a railroad is still subject to various orders of the ICC during reorganization, there are some important exceptions:

Except with respect to abandonment under § 1170 of this title, or merger, modification of the financial structure of the debtor, or issuance or sale of securities under the plan, the trustee and the debtor are subject to the provisions of title IV of title 49 that are applicable to railroads and the trustee is subject to orders of any Federal, State, or local regulatory body to the same extent as the debtor would be if the petition commencing the case under this Chapter had not been filed . . .

11 U.S.C. § 1166 (emphasis added).

Thus, even in a railroad reorganization, a merger, modification of the debtor's financial structure, or issuance or sale of securities is excepted from federal or state regulatory control, and the approval of such restructuring transactions is a matter for the bankruptcy court alone. 5 Collier on Bankruptcy, ¶ 1166.01, at 1166-2 (15th ed. 1988). Similarly, jurisdiction over abandonment of railroad lines was also transferred from the ICC to the bankruptcy court under Chapter 11. 11 U.S.C. § 1170.

The Bankruptcy Code's constriction of the role of regulatory agencies in reorganization plans from that under the prior law is also reflected in the Bankruptcy Code's treatment of the Securities and Exchange Commission ("SEC"). Under former Chapter X, the SEC played a broad, pivotal role in the plan confirmation

process. This role was all but eliminated under the Bankruptcy Code.

Under the Bankruptcy Act, the court was required to submit a plan of reorganization to the SEC where the indebtedness of the debtor exceeded \$3,000,000. 11 U.S.C. § 572 (repealed). The Bankruptcy Act further provided that where the debtor's assets exceeded \$3,000,000, the court could not approve a plan until the SEC had issued its report, or notified the court that no report was forthcoming, or the time for filing a report had expired. 11 U.S.C. § 574 (repealed). Although the SEC's report was to be advisory only, its great experience, skill and thoroughness in such matters gave its reports considerable weight. 6 Collier on Bankruptcy ¶ 7.36, at 1305 (14th ed. 1978) (footnote omitted).

Some who testified before Congress supported preserving the SEC's broad role in the approval of corporate reorganization plans. See, e.g., Hearings on H.R. 31 and H.R. 32 (Bankruptcy Act Revision) Before the Subcomm. on Civil and Const. Rights, House Judiciary Comm., 94th Cong., 2d Sess., Ser. 27, at 1880-81 (1976) ("Hearings") (Statement of Harvey R. Miller, William J. Rochelle, Jr and J. Ronald Trost on behalf of the National Bankruptcy Conference on business reorganizations); 1903-04 (Statement of Arthur L. Moller and Herbert Katz on behalf of the National Conference of Bankruptcy Judges). Congress, thus clearly aware of the issue, chose instead to eliminate the

Bankruptcy Act requirements of SEC review in the plan process and the attendant delays. Instead, the SEC's only remaining role under the Code is in section 1109(a), which permits the SEC to "raise and . . . appear and be heard on any issue in a case under this chapter . . ." 11 U.S.C. § 1109(a).

Thus Congress made a sweeping and fundamental policy decision, reflected in these changes from the predecessor statutes: To reduce non-bankruptcy regulatory control over plans, avoid or minimize fractionated, multi-jurisdictional plan review or approval, and centralize the plan approval process in the bankruptcy court.

It is simply disingenuous to suggest that, even though Congress reduced federal and state regulatory control over railroad reorganization plans and the role of the SEC in corporate reorganization plans generally, the Code is somehow unclear on whether state regulators still have a veto over public utility reorganization plans. Rather, it is more consistent with the deregulatory fabric of the Code to conclude that the repeal of the prior statutory veto power over public utility plans means that while a public utilities commission has a right to appear and be heard, Congress intended to limit regulatory review to rate changes provided in a plan, as expressly provided in 11 U.S.C. § 1129 (a)(6).

The Legislative History of the 1978 Code

The legislative history of the 1978 revision confirms that the reduced role of state regulatory agencies in utility reorganization plans was no aberration. Rather, in light of the dramatic reductions of the ICC's role in railroad reorganization plans and the SEC's role in corporate reorganization plans, the elimination of the requirement of regulatory approval for public utility plans is properly viewed as part of a broad fabric of reduced regulatory control. As the legislative history makes clear, Congress determined that the delays involved in requiring multiple determinations on the merits of proposed plans, *i.e.*, of both a regulatory agency (or agencies) and the bankruptcy court, were unnecessary, and that the bankruptcy court was not only fully capable of resolving the competing interests presented in a reorganization case, but also the best, neutral forum for doing so. Regulatory agencies could advocate their views regarding particular plans before the bankruptcy court but could not control the plan outcome.

It was the federal non-bankruptcy regulators that provided the examples most often used in the congressional debate on this point. That debate clearly reflects the conscious choice made by Congress to remove the extraneous layers of bureaucratic review from reorganization proceedings. The role of the ICC in bankruptcy proceedings became a common, and timely, topic, for

the 1970's saw a number of railroad reorganizations in the Northeast and industrial Midwest. (In contrast, public utility bankruptcies were understandably not a topic of much explicit discussion in the legislative history of the Bankruptcy Code because at that time there had not been a public utility bankruptcy in 40 years.)

The debate about regulatory control over railroad reorganizations focused on questions of expertise, duplication, and the proper role of the "public interest" and its advocates. The ICC supported an increased regulatory role in railroad reorganizations. Echoing the arguments that may be advanced today in support of S.46, the ICC argued that bankruptcy courts did not have the time, staff or expertise to evaluate railroad operations, and that the ICC should therefore pass upon a railroad's "ability to continue to provide needed public services." Hearings at 2580 (Statement of ICC Chrm. George M. Stafford).

The ICC recognized that, under prior law, there had been considerable duplication of effort between itself and the reorganization court and proposed eliminating the duplication, "by giving the ICC the primary role in the transportation and procedural aspects of rail reorganizations while giving the courts essentially a review function" Hearings at 2585-86; see also 2592.

The thrust of any amendment should be toward less judicialization of the process, not more.

We must take issue with the Bankruptcy Commission's view that the essential purpose of section 77 is the protection of creditors' rights . . . railroad reorganization must involve equal considerations of the public's interest in continued rail service.

Hearings at 2590 (emphasis added). The ICC opposed the proposals to reduce its role in railroad reorganization plans -- proposals which were eventually enacted into law -- because

it would introduce into railroad reorganization law an escalation of private rights, as compared to the equality between public and private interests recognized by the Supreme court in the New Haven Inclusion Cases, supra [399 U.S. 392, 90 S.Ct. 2054, 26 L. Ed. 2d 691 (1970)]

Hearings at 2580.

Congress did not, however, appear willing to adopt readily the view that the ICC, as advocate of the public interest in rail service, was the right agency to conduct an impartial balancing of the public interest which it advocated and the rights and interests of creditors and shareholders. Thus, committee counsel Klee asked ICC Chairman Stafford:

Mr. Klee: [I]f the Interstate Commerce Commission is the advocate of protecting the public interest, and if in a railroad reorganization the public interest is to be balanced equally, as you testified, with the rights of creditors and stockholders, then as a matter of fairness is it not better to have an independent court, which will develop expertise and will not have crowded dockets, weight the arguments of the Interstate

Commerce Commission, representing the public interest, against the argument of the creditors in determining whether a plan is fair and equitable?

In this regard I call to your attention section 9-503 of H.R. 31 [enacted as 11 U.S.C. § 1173(A)(4)] which incorporates as a requirement of confirmation, protection of the public interest.

Chairman Stafford: Well, we think the creditors rights are also a part of the public interest when we rule on any case that we have. So, it's not a case of our just ruling on the consumer side, and forgetting about the financial interests on the other side. We have been doing this, in our judgment, rather well for many years.

Hearings at 2611-12. The Committee was not persuaded.

The concerns expressed by committee counsel about allowing the same regulatory agency, which normally acts as the advocate of the public interest, to act also as an adjudicator in balancing such interests against the interests of investors, applies with equal force to state regulatory agencies. Such a concern has become heated in the Public Service Chapter 11 case, for example, by published statements of New Hampshire state officials, repeatedly characterizing creditors and shareholders as "greedy Wall Street investors." The potential for such adverse influence on the adjudicatory process suggests why Congress saw fit to reduce the role of state regulatory agencies, while increasing the control of the politically independent bankruptcy court over the plan adjudicatory process and the related balancing of interests.

Moreover, it is not necessary to give an agency a veto power in order to draw on its dedication and expertise or to obtain the benefit of its advocacy of the public interest. The National Bankruptcy Conference, which supported giving the ICC a role analogous to that of the SEC in corporate reorganizations, illustrated how such a role would work:

No one doubts that the Commission, which has a responsibility to protect the public interest in rail transportation, can and should make a contribution to the resolution of the problems of a railroad in reorganization. It can, and I am sure would, continue to do so, making its expertise and its knowledge of the public interest available to the courts. Both bills recognize that it is to be a party in interest, with standing to appear and be heard.

[The NBC's recommendations are] designed to be sure that the railroad reorganization process is, in the final analysis, the responsibility of the bankruptcy court, and not subject to being short-circuited by other agencies.

Hearings at 2595 (Statement of Charles A. Horsky on behalf of the National Bankruptcy Conference) (emphasis added).

Others who testified before the Subcommittee agreed that the bankruptcy court should be the sole reorganization forum, and that the applicable regulatory agencies and the public interest they represent would be treated fairly by that court. Joseph C. Simpson, vice president-investment counsel for Metropolitan Life Insurance Co., testified that

We think the State agencies, the Department of Transportation, and the Interstate Commerce Commission will get fair consideration by the bankruptcy court of the problems they are trying to press for in the public interest. In fact, we find the courts are most sympathetic when considering the public interest side of any question.

.

We feel it is desirable to restrict regulatory controls [during the proceeding] rather than expand them.

During the reorganization proceeding, a main objective of the trustee is to deal with those problems that caused the railroad to go into bankruptcy in the first place. There are usually many such problems. Many believe that railroad bankruptcies are often due at least in part to governmental restrictions and regulatory problems. So that any restraint of State agencies' influence over the bankruptcy court and over the trustee will be helpful.

Hearings at 1634-35 (emphasis added).

Thus, in its 1978 overhaul of the bankruptcy laws, Congress was confronted by diverse opinion that fully illuminated all the issues. After careful consideration of these views, Congress consciously embraced a blueprint of reduced regulatory control for its revision of the law.

The Balance of Federalism

Viewed in perspective, this framework for reorganization proceedings represents a very limited interference with state

regulatory powers: it applies only to transactions provided in the plan. The operations of the debtor in possession outside of a plan remain subject to state and local regulatory laws, with certain limited exceptions.^{1/} Similarly, operations after a plan's effective date must comply with applicable state regulations, again with limited exceptions, such as laws relating to financial condition that would impact upon the reorganized debtor's operations under the plan. 11 U.S.C. § 1142(a). A provision such as section 1123(a)(5), limited as it is to the corporate restructuring under a reorganization plan, is hardly a wholesale intrusion on state regulatory powers. Indeed, the Code specifically exempts the authority of federal and state regulators over utility rates from control by the bankruptcy court. That is, what apparently should be the greatest concern of the sponsors of S.46 -- the control of state regulators over retail ratemaking -- is left undisturbed by even the streamlined procedures of Chapter 11.

Moreover, even the presumption of state authority is limited to the situation where the federal interest in reorganization and

^{1/} These exceptions include those for laws pertaining to financial condition (11 U.S.C. § 363(1)), laws which discriminate on the basis of nonpayment of prepetition debt (*id.* § 525(a)), and actions which violate the automatic stay and are not excepted by 11 U.S.C. § 362(b)(4)-(5). The application of state and local regulatory laws to trustees and debtors in possession may also be limited by the equitable powers of the Bankruptcy Court under 11 U.S.C. § 105.

rehabilitation embodied in the bankruptcy laws is most acute. After all, the Constitution explicitly gives the federal government the authority to "establish ... uniform laws on the subject of bankruptcies throughout the United States." U.S. Const. art. I, § 8. The entire purpose of a Chapter 11 case grows out of this federal bankruptcy responsibility: enabling a debtor to restructure its affairs under a plan.

The Bankruptcy Code comes into play with respect to a public utility when the state regulatory scheme has failed to balance the interests of creditors, shareholders, and the public and to preserve the financial integrity of the utility. Confirmation of a plan is the climax of the federal reorganization process. Given this, it was prudent for Congress to determine that interests of centralized, expeditious administration justify a statutory scheme which (i) avoids the delays and fragmented decision-making inherent in multijurisdictional oversight of transactions under a plan, and (ii) avoids leaving restructuring transactions under a plan subject to the veto power of regulatory schemes or agencies which failed to protect the debtor's financial integrity in the first place. Cf. Hearings at 1634-35 ("Many believe that railroad bankruptcies are often due at least in part to governmental restrictions and regulatory problems [s]o that any restraint of State agencies' influence over the bankruptcy court and over the trustee will be helpful.") (testimony of Joseph C. Simpson).

The Impact of S.46

Under S.46, any regulatory agency with jurisdiction over any transaction under the reorganization plan of a utility could bring the plan process to a grinding halt. At best, requiring such piece-meal plan approval by all interested agencies could result in substantial delays -- delays that could be fatal and which are not justified by any reorganization policy or fair view of federal-state relations. At worst, a plan could be stymied by inconsistent or conflicting rulings of the different agencies claiming jurisdiction, i.e., one agency might approve the transaction while the other disapproved it or they might place inconsistent conditions on their approval of the transaction.

Operating under the regime of this bill, the bankruptcy court will not be free to exercise its unbiased and balanced judgment of what measures are appropriate to return an ailing company to a sound footing. Rather, the court will be forced to appease a non-bankruptcy regulatory bureaucracy that cannot take the broader view of the bankruptcy court, but must advance its own discrete mission.

In the final analysis, non-bankruptcy regulatory approval begins to encrust reorganizations once again with the endless proceedings Congress sought to eliminate in 1978. Only those who benefit from legal proceedings themselves -- as opposed to those who stand to benefit from a reorganized and rejuvenated company

-- can benefit from S.46's proposed abandonment of the modern process of corporate reorganizations. Delay in reorganization proceedings depletes a company's resources to the detriment of those really concerned -- the company, its investors, its employees, and its customers.

And we must remember, Mr. Chairman, that the proponents of S.46 do not really offer us anything for this disruption of the reorganization process. Contrary to their claims, it cannot be seriously maintained that S.46 is "pro-consumer." With respect to the setting of rates, the Bankruptcy Code preserves the governing law outside the context of bankruptcy. That is, state public utilities commissions still must approve retail rates for a reorganized utility, while the Federal Energy Regulatory Commission ("FERC") must approve wholesale rates.

Indeed, under the existing Code, the state public utilities commission remains the ultimate gatekeeper to retail rates and the marketplace. No utility -- whether a thriving company or a reorganized bankrupt -- can collect any rates without the approval of the state commission. Thus, the interests of consumers of electrical power are hardly left unprotected. If this bill's sponsors' real complaint is with the division of regulatory authority between FERC and state commissions, their concerns are more appropriately considered in the context of the

statutes governing the regulation of energy and within the committees of the Congress having jurisdiction over them.

THE RETROACTIVE EFFECTIVE DATE OF S.46 IS UNFAIR
AND INCONSISTENT WITH CONGRESSIONAL PRACTICE

In addition, Mr. Chairman, S.46 explicitly provides that "(t)his Act and the amendments made by this Act shall become effective on the date of enactment and shall apply to any case pending on such date." The bill unmistakably seeks to change the rules in a judicial proceeding while that proceeding is ongoing. Regardless of the issues surrounding the substantive provisions of the legislation, its retroactive effective date offends any common sense understanding of fairness.

The American legal tradition has historically viewed retroactive legislation as objectionable because it deprives citizens of the ability to plan their conduct with reasonable certainty of the legal consequences. A common example of our hostility towards retroactive law is the constitutional provision that prohibits the application of ex post facto law.

Another example of the bias against retroactive law is the rule of statutory construction that a retroactive operation will not be given to a statute unless the legislature manifests such an intention clearly on the face of the statute. See Union Pacific R. Co. v. Laramie Stock Yards Co., 231 U.S. 190, 199 (1913); United States Fidelity & Guaranty Co. v. United States ex

rel. Struthers Wells Co., 209 U.S. 306, 314 (1908) ("The presumption is very strong that a statute was not meant to act retrospectively, and it ought never to receive such a construction if it is susceptible of any other.").

Where the retrospective operation of a statute interferes with property or contract rights, it may run afoul of the fifth amendment, either as an uncompensated taking or as a denial of due process. Indeed, in United States v. Security Industrial Bank, 459 U.S. 70 (1982), the Supreme Court construed a bankruptcy lien avoidance statute to have no retroactive application in order to avoid these constitutional pitfalls. See also Louisville Joint Stock Land Bank v. Radford, 295 U.S. 555 (1935); Holt v. Henley, 232 U.S. 637 (1914). Whether S.46, if enacted, will suffer from serious constitutional flaws on such grounds depends upon the form in which it is passed and the stage of the affected bankruptcy proceedings at that time.

Perhaps more importantly, the retroactive application of S.46 is at odds with a purposeful and long-standing congressional practice that has largely avoided changing the rules in ongoing bankruptcy proceedings -- a practice that has prevented bankruptcy law from becoming a political pawn. For example, in the massive overhaul of the bankruptcy laws that produced the Bankruptcy Code of 1978, Congress took pains to provide that:

[a] case commenced under the Bankruptcy Act, and all matters and proceedings in or relating to any such case, shall be conducted and determined under such Act as if this Act had not been enacted, and the substantive rights of the parties in connection with any such bankruptcy case, matter, or proceeding shall continue to be governed by the law applicable to such case, matter or proceeding as if the Act had not been acted.

Pub. L. No. 95-598, §403, 92 Stat. 2683 (1978)(as amended by Pub. L. 98-353, §382 (1984))(emphasis added). In adopting this transitional provision, Congress expressed its preference for "the orderly transition from the current bankruptcy law," as well as a respect for traditional congressional practice. See H.R. Rep. No. 595, 95th Cong., 1st Sess., at 288 (1977)("There is precedence for this treatment of pending cases. On the effective date of the amendments made by the Chandler Act in 1938, all pending cases were left to proceed under the previously existing law.")

More strikingly, a comprehensive review of the 115 bankruptcy acts Congress passed between 1800 and 1976 reveals only 11 examples of a change in the law -- either as a discrete provision or as a whole bill -- made applicable to pending cases. An even more detailed scrutiny of congressional practice in the last 20 years underscores the antipathy of Congress to retroactive bankruptcy legislation. Of the 293 bankruptcy bills introduced during those ten Congresses, only 11 even proposed that some provision be retroactively effective. During that

time, only one permanent amendment to the Bankruptcy Code containing a retroactive provision became law and that was a minor subsection of the massive Bankruptcy Amendments and the Federal Judgeship Act of 1984.

In short, by seeking to change the law governing a pending matter, S.46 departs from any standard of fairness and marks an unwarranted departure from sensible congressional practice. By changing the rules in the middle of the game, and now requiring state approval of its reorganization plan, S.46 defeats PSNH's expectations of effectuating an expeditious and orderly reorganization. And there is no principled reason offered by the proponents of S.46 on behalf of its retroactive application when Congress so rarely enacts retroactive bankruptcy legislation. All that comes to mind to justify a retroactive bill here is the fact that its sponsors do not like one possible outcome of an ongoing judicial proceeding. This seems an insufficient reason to take steps to apply such a drastic change retroactively.

S.46 -- THE UNNECESSARY STRATAGEM

Finally, Mr. Chairman, it is important to note here that events have passed by even the narrow, self-interested goal of this bill. S.46 was originally "prompted" by the Public Service bankruptcy because one result of these proceedings might have been a restructured Public Service that was beginning to receive

some return on its Seabrook investment before Seabrook was in commercial operation. By giving the NHPUC authority to approve the restructuring transactions under Public Service's plan, S.46 effectively gives the state the power to block the reorganization.

However, events have moved beyond this original point. Low-power testing has been completed and knowledgeable observers -- such as the chairman of the NHPUC -- believe that Seabrook will begin commercial operations soon, perhaps as early as spring 1990. With that result being likely, the original reason for this bill disappears. The state's law prohibiting a return on construction work in progress ("CWIP") has no application once Seabrook is operational, and prudent investment in that project may be recouped. In that situation, S.46 will hardly be a meaningful vindication of New Hampshire's anti-CWIP policy.

Most importantly, published reports indicate that the negotiating positions of the parties, including the state, have significantly narrowed. It is entirely possible that the parties will reach a consensus on a reorganization plan and agree to a fair rate increase. However, even if negotiations ultimately break down, all interested parties, including the state, may submit competing reorganization plans and be heard in the normal bankruptcy process. How all the issues would be resolved cannot

be known in advance, but they would be resolved by a neutral bankruptcy judge following fair and well-established procedures.

In short, even accepting as appropriate the notion that legislation may be used to advance the interests of one party to a judicial proceeding, S.46 does not appear to advance those parochial interests any longer. Truly, S.46 would disrupt the whole structure of Chapter 11 reorganization proceedings for no reason, much less any good reason.

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ROBERT J. CYNKAR

August 22, 1989

BY MESSENGER

The Hon. Howell Heflin
Chairman, Subcommittee on Courts
and Administrative Practice
Senate Judiciary Committee
223 Hart Senate Office Building
Washington, D.C. 20510

Attn: Karen Kremer

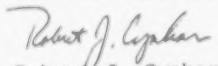
Re: S.46

Dear Mr. Chairman:

Enclosed are the responses of Richard Levin to the additional questions submitted by the Subcommittee on Courts and Administrative Practice concerning S.46. If any additional questions are raised or other information is needed, please do not hesitate to have your staff contact me.

I would also like to take this opportunity, on behalf of the Public Service Company of New Hampshire, once again to thank you and your staff for all your courtesies in putting together the hearing on S.46. As you know, we strongly question the wisdom of this bill and have appreciated the opportunity to explain the serious problems we see with this legislation. We look forward to working closely with you and the Subcommittee in any future work on this legislation.

Sincerely yours,


Robert J. Cynkar

RJC:vm

Enclosure

Responses By Richard Levin
to Questions Submitted by the Subcommittee on Courts
and Administrative Practice Concerning S.46

QUESTIONS SUBMITTED BY SENATOR HEFLIN

1. IF IN FACT YOUR INTERPRETATION OF 1123 (a) IS CORRECT,
WHAT IS TO PREVENT UTILITY COMPANIES FROM FILING CHAPTER
11 PETITIONS TO CIRCUMVENT THE STATE REGULATORY PROCESS?

ANSWER

At the outset, it is important to remember that the whole purpose of the bankruptcy laws is to suspend normal business demands while a failing corporation is reorganized. Therefore, the basic goal of any bankruptcy system in one sense must be to, at least temporarily, "circumvent" common legal process. The automatic stay provisions of the Bankruptcy Code, for example, halt many creditor actions under state law, and could be said to "circumvent" the various state laws governing creditor-debtor relations. However, such a result is entirely consistent with the fundamental logic of bankruptcy law. Moreover, it clearly advances the constitutional mandate that Congress establish "uniform laws on the subject of bankruptcies throughout the United States." U.S. Const. art. I, § 8. Indeed, the terms of section 1123(a) no more "circumvent" state regulatory process than they "circumvent" the process of the Securities and Exchange Commission or the Interstate Commerce Commission, which also do not have approval authority over a reorganization plan.

In addition, I find it hard to imagine a situation in which a corporation would file for reorganization in bankruptcy solely

to avoid some state regulatory process. Outside of the impact on a company's standing in the marketplace of a declaration that it is bankrupt, the bankruptcy process itself imposes many burdens on a company and is not subject to control by the debtor-in-possession. It is the independent judgment of the bankruptcy court, with input from many interested parties, that governs the outcome of reorganization proceedings. A reorganized company may look very different from the entity that originally petitioned for Chapter 11 reorganization. Thus, a bankruptcy proceeding is not in any meaningful way an attractive option for a company not truly in dire financial straits.

On the contrary, most businesses labor mightily to stay out of bankruptcy. This certainly was true in the case of Public Service Company of New Hampshire. Indeed, the "risky" financing criticized by some at the hearing was sought in 1984 as a last-ditch effort to avoid bankruptcy.

Beyond the practical unlikelihood of the bankruptcy process being used solely to circumvent the state regulatory process, the Code itself provides a safeguard against the abuse of the bankruptcy process. An independent federal bankruptcy judge presiding over reorganization proceedings will not approve a plan, especially one that proposes significant restructuring of a company, unless that course is truly a proper way to resolve the bankruptcy. Even more specifically, section 1112(b) allows the

bankruptcy court, upon the motion of a party, to dismiss a Chapter 11 case "for cause," and provides a non-exhaustive list of what may be included in "cause." Though not enumerated in that list, it is clear that "'[c]ause' for dismissal ... of a Chapter 11 case includes the absence of 'good faith.'" 5 Collier on Bankruptcy ¶ 1112.03 at 1112-26 (1989). See also In re Victory Constr. Co., Inc., 9 Bankr. 549, 558 (Bankr. C.D. Cal. 1981) ("'Good faith' must ... be viewed as an implicit prerequisite to the filing or continuation of a proceeding under Chapter 11 of the Code."). As one commentator put it, "Circumventing jurisdictional restrictions, a frivolous purpose absent any economic reality, the use of the statute for purposes of malicious delay, or other ulterior purpose are all apprehended by the good faith test." Ordin, "The Good Faith Principle in the Bankruptcy Code: A Case Study," 38 Bus. Law. 1795, 1796 (1983).

A Chapter 11 petition filed for the purpose of circumventing the state regulatory process when a company is not in genuine financial distress would, it seems to me, be open to a motion to dismiss under section 1112(b) on grounds of bad faith. "[O]ne who invokes the protective provisions of the bankruptcy laws must do so in order to accomplish and further the expressed legislative aim of the particular Chapter and not for any other purpose." In re Moqui, 17 Bankr. 680, 681 (Bankr. M.D. Fla. 1982).

For example, the good faith doctrine was used in In re Smith, 58 Bankr. 448, 451 (Bankr. W.D. Ky. 1986) to block "the use of federal bankruptcy law to defy legitimate state ends." There, the bankruptcy court held that it is not "permissible for a financially sound debtor to invoke Chapter 11 to avoid posting a supersedeas bond in pending state court litigation." Id. at 449.

In sum, even if there was, in a particular case, an incentive to abuse the bankruptcy process as suggested by this question, the bankruptcy laws contain their own safeguards against a meritless Chapter 11 petition filed for some ulterior motive. When a petition is filed on behalf of a company genuinely needing reorganization, if not liquidation, it is quite simply the explicit goal of the bankruptcy process to stop the normal operations of the marketplace, to suspend state and federal regulatory mechanisms, and even to halt certain judicial processes, in order to create the "breathing space" that will allow a bankrupt company to be put back on a sound footing. Reorganization in bankruptcy, after all, is drastic treatment for a company, a kind of emergency incubation to resuscitate its economic vitality.

2. THERE IS GREAT CONCERN THAT BY ALLOWING PSNH TO REORGANIZE AS A HOLDING COMPANY, PARTLY UNDER FERC'S JURISDICTION, THAT THE BURDEN OF FINANCING THE SEABROOK PLANT IS SHIFTED FROM THE STOCKHOLDERS, TO THE RATEPAYERS OF NEW HAMPSHIRE. HOW DO YOU RESPOND TO THIS CONCERN?

ANSWER

Under well-established principles of law, a utility is entitled to a fair and reasonable return on all capital prudently invested in a plant. That return, of course, comes from rates paid by the customers of the utility. If a management decision to build a plant was prudent when made, the financial risks of that decision -- along with the benefits of the power produced by that plant -- are passed to ratepayers. This seems to me to be an obviously fair system.

In short, ratepayers would ultimately pay under any system -- state or federal -- but only after regulators conclude a capital investment was prudent. And the investment in Seabrook has been found to be prudent by the outside auditors hired by the New Hampshire Public Utilities Commission ("NHPUC") to evaluate the Seabrook project. In 1987, these auditors were able to report:

Seabrook Station was generally managed in an effective manner that minimized the total controllable cost of the project while maintaining an emphasis of quality and safety. These objectives of building a high quality, safe facility at a reasonable cost and in accordance with an established schedule were defined early in the project and served to support the subsequent approach developed to manage Seabrook Station.

The auditors believed that only certain limited costs -- 6.9 percent of the total -- could have been minimized by more effective management, and so concluded:

With the exception of [this] amount . . . , PSNH was found to have managed the Seabrook Station project in an effective fashion and in a manner that was consistent with the need to complete a high quality and operable facility capable of safely meeting the power demands of New England.

Perhaps even more importantly, New Hampshire has always recognized the need for Seabrook and remained a strong supporter of it. Indeed, in 1981, just after the accident at Three Mile Island, the New Hampshire Legislature passed a resolution urging that, as long as appropriate safety measures were followed, "the Seabrook nuclear power plant should be completed and brought to full generating capacity as quickly as possible." More recently, in a 1985 decision approving a PSNH effort to secure additional financing for Seabrook, the NHPUC recognized once again that PSNH must have additional generating capacity to serve the needs of the citizens of New Hampshire and New England. [In re: Public Service Company of New Hampshire, DF 84-200, at 40-41.] The NHPUC concluded that "Seabrook completion is the best alternative for meeting PSNH's capacity requirements," [id. at 41] and that "Seabrook is the least cost alternative in all cases." [id. at 42.]

In short, through their representatives, New Hampshire ratepayers have embraced the investment in Seabrook as an efficient step to meet their growing energy needs and have critically evaluated that investment to ensure that it represents money well spent. It is only fair -- as the law so clearly recognizes -- that the beneficiaries of Seabrook pay for it through their rates.

Of course, even when the prudence of investment in an operational plant is established, there remains the question of how the costs of construction work in progress ("CWIP") for an unfinished plant should be accounted for in rates. Given the requirement that prudent investment be compensated, state regulators have had two options in accounting for CWIP, each having different practical implications. The majority of states and FERC permit utilities to recover some, or all, of the costs of CWIP in rate base. Under this policy, ratepayers are paying for a new facility before they are actually receiving power from it. However, as a result of this approach, rates rise more slowly over time, rather than increasing dramatically when a new power plant comes on-line. In addition, because rates begin to compensate a utility for its investment while construction is underway, less financing is needed, and the overall cost of the new facility is lower.

A minority of states, including New Hampshire, do not include CWIP costs in rate base before a new plant is operational. Ultimately though, when a new plant becomes operational, a reasonable return on prudent investment must be paid even in these jurisdictions. In addition, a utility is allowed to recover an allowance for funds used during construction, which includes interest payments on debt financing and dividend payments to shareholders.

For a new plant that becomes operational -- as even Senator Rudman has recognized Seabrook will soon be -- CWIP essentially is a question of timing: when should ratepayers begin to pay for a new power plant, while it is under construction, or after it begins to produce power? In this situation CWIP does not -- constitutionally it cannot -- raise a question of whether a utility will be given a reasonable return on such an investment at all. And in this case, when Seabrook is likely to be in commercial operation before the bankruptcy proceedings are concluded, even the question of timing falls away. The citizens of New Hampshire will soon receive the benefits of Seabrook, and the bill is now coming due. The restructuring of Public Service as part of its reorganization in bankruptcy will have no effect on the fact that ratepayers must pay for an operational Seabrook.

At the same time, New Hampshire's anti-CWIP law has had a decided impact on the stockholders of Public Service. By

December 1988, the approximately \$2.4 billion Public Service had invested in Seabrook represented the vast majority of its total assets, and, most critically, assets on which it could not yet earn any return because of the anti-CWIP law. As a result, in spite of alternative financing efforts, Public Service suffered severe cash-flow shortages that ultimately drove it into bankruptcy.

This bankruptcy will hardly leave those who invested in Public Service unscathed. Indeed, as a result of the extraordinary burden imposed by New Hampshire law on the construction of Seabrook, investors in Public Service will lose over \$1 billion. At the same time, under that same New Hampshire law, it is now appropriate for ratepayers, through just and reasonable rates, to pay for the cost of Seabrook.

3. IF WE ACCEPT YOUR INTERPRETATION OF SECTION 1123(a), HOW WILL THE PUBLIC INTEREST BE PROTECTED WHEN UTILITIES FILE FOR BANKRUPTCY?

ANSWER

If the Subcommittee does not accept my understanding of section 1123(a), and believes that the Code still requires state regulatory approval of reorganization plans, then S.46 is a truly pointless bill, for the "change" it proposes would merely be a restatement of existing law. The Subcommittee would be concluding that the Bankruptcy Code as written requires the procedure proposed by S.46. In that case, it would appear that the most sensible course for the Subcommittee would be to wait for the judicial process to be completed before any further action is taken. After all, the bankruptcy court in the Public Service Chapter 11 proceedings has this question before it but has not yet ruled, and its ultimate ruling could be appealed to higher courts. Until a final judicial pronouncement is made as to what the current version of the Code requires -- and the courts have concluded which interpretation is correct -- it makes no sense to restate or to change the law, solely because one litigant, Public Service, has made an argument with which the Subcommittee disagrees.

In all honesty, though, a fair examination of the Code and its legislative history -- as I have tried to present in my

prepared statement -- leads inexorably to the conclusion that our view of section 1123(a) is correct. And as that legislative history shows, Congress in 1978 was far from unconcerned about vindicating the public interest in bankruptcy proceedings. As I said in my statement, the distinctive mission of the bankruptcy court in Chapter 11 proceedings -- a mission by definition beyond the expertise and role of any other state or federal regulatory agency -- is solely devoted to undertaking an impartial balancing of all the public and private interests implicated in the effort to put a bankrupt company back on its feet.

Thus, in terms of the public interest in bankruptcy proceedings -- and the harmonization of the subsidiary interests embraced in such proceedings -- it is the bankruptcy court that is the guardian. As designed by Congress in 1978, the bankruptcy court can exercise unbiased and balanced judgment of what measures, consistent with the public interest, are needed to rehabilitate a failing company. Indeed, a fundamental principle embodied in Chapter 11 is that restoring a troubled company to economic vitality is very much in the public interest. When other state or federal agencies have a veto over reorganization proceedings, the bankruptcy court is forced to appease a non-bankruptcy regulatory bureaucracy that cannot take the broader view of the court, but must advance its own discrete mission. At the same time, the unique ratemaking expertise of federal and state regulators is preserved by the requirement that

they approve any rate changes that come out of the reorganization process.

Moreover, by giving the bankruptcy court the dominant role in Chapter 11 proceedings, Congress advanced the public interest in the expeditious reorganization and rehabilitation of bankrupt companies. Centralized adjudication avoids the delays and fragmented decision-making inherent in multiple determinations on the merits of proposed reorganization plans. Control by the politically independent bankruptcy court, finally, helps to insulate the adjudicatory process from adverse parochial influences, and thus assure the public of a truly fair bankruptcy system beyond the manipulation of political interests.

5. THE PROPOSED REORGANIZATION OF PSNH IS AN ATTEMPT TO ALLOW PSNH TO RECEIVE SOME RETURN ON ITS INVESTMENT BEFORE THE PLANT BECOMES OPERATIONAL. BUT AT THE SAME TIME IT IS MY UNDERSTANDING THAT THE PUBLIC UTILITY COMMISSION WILL RETAIN CONTROL OVER THE RATES OF ELECTRICITY SOLD AT RETAIL TO THE PUBLIC.

IF THAT IS SO, HOW DOES PSNH BENEFIT FROM THIS ARRANGEMENT?

ANSWER

As I explained in my answer to Question No. 2 above, it is now likely that Seabrook will enter into commercial operations next year, perhaps before the bankruptcy proceedings are concluded. As a result, the determination of future rates is no longer necessarily premised on Public Service receiving a return on its Seabrook investment before it is operational. Thus, one important goal of the original plan of reorganization proposed by Public Service has become moot.

However, if that were still a goal, then the proposed reorganization would permit Public Service to include a portion of its Seabrook investment in wholesale rates for the power it would sell to its new retail sister corporation. While the NHPUC might not permit the retail company to pass through all of these costs, the current costs of power in New England strongly suggest that the PUC would have to permit pass-through of a significant portion. Public Service would thus receive some benefit from the new arrangement pending Seabrooks's operation.

6. SENATOR HUMPHREY IN HIS INTRODUCTORY REMARKS INDICATED THAT CONGRESS IN THE MUNICIPAL BANKRUPTCY AMENDMENTS WHICH WERE PASSED LAST YEAR ADOPTED A PROVISION REQUIRING THAT ALL NECESSARY REGULATORY APPROVALS UNDER APPLICABLE NON BANKRUPTCY LAW BE OBTAINED BEFORE A PLAN OF MUNICIPAL DEBT ADJUSTMENT COULD BE CONFIRMED. HE ARGUES THAT S.46 IS MERELY BUILDING UPON THAT PROVISION. HOW DO YOU RESPOND TO THIS STATEMENT?

ANSWER

An Act to Amend the Bankruptcy Law to Provide for Special Revenue Bonds, and for Other Purposes, Pub. L. No. 100-597, 102 Stat. 3028 (1988) (the "Municipal Bankruptcy Amendments") did make a series of amendments to Chapter 9 of the Bankruptcy Code, the provisions governing the very specialized circumstances of a municipality in bankruptcy. Those circumstances are so different from those of a business corporation that legislation providing for the adjustment of the debts of a municipality in bankruptcy was first enacted only in 1937. See 4 Collier on Bankruptcy, ¶ 900.01, at 900-1 (1989). Those unique circumstances have required a specially tailored bankruptcy regime for municipalities. As Collier's explains:

Municipal bankruptcy is unlike bankruptcy for individuals or private corporations. Because of the public nature of the entity experiencing financial difficulties, there is no provision in the law for liquidation of its assets and distribution of the proceeds to creditors. Nor does it seem possible that there could be such a provision. The dissolution of a public entity under the bankruptcy laws, even with the active consent and participation of the officials of that entity, could run afoul of the tenth amendment to the Constitution, and the reservation

to the states of sovereignty over their internal affairs. Even though the Supreme Court has upheld municipal bankruptcy legislation generally, it has done so at least in part on the premise that the legislation involves no possibility of adjudication of a municipality as a bankrupt and liquidation of its assets. Notwithstanding the broad power which the Supreme Court has acknowledged resides in Congress with respect to bankruptcy legislation, it is doubtful that any such liquidation provision would be upheld.

Thus, the purpose of municipal bankruptcy legislation must be directed toward a reorganization of its financial affairs, or, as the statutory title states "adjustment of its debts." . . .

The main differences, however, arise in the conduct of the case. Because of the severe limitations placed upon the powers of the court in a municipal debt adjustment proceeding, required by the tenth amendment and the Supreme Court's decisions in the cases upholding municipal bankruptcy legislation, the court is far less involved in the conduct of a municipal bankruptcy case and in the operation of the municipal entity during the time that its financial affairs are undergoing reorganization. The court has no power to control expenditures for municipal services or any other activities of the municipal entity.

Id., ¶ 900.02, at 900-9 - 11.

Congress explicitly recognized the distinctive nature of a municipal bankruptcy when it passed the Municipal Bankruptcy Amendments in 1988. As the Senate Judiciary Committee explained:

Municipal systems are often also subject ... to political requirements, unique to governments, such as voter approval of additional debt. Some have expressed a concern that a failure to make a plan subject to requirements of this sort could override state and

local financial and political controls and raise constitutional issues as to the scope of the bankruptcy power that need not be resolved to further sound municipal bankruptcy policy.

S. Rep. No. 506, 100th Cong., 2d Sess. 11 (1988). See also 133 Cong. Rec. S16231 (daily ed. Nov. 12, 1987) (statement of Sen. DeConcini).

The House Judiciary Committee noted the practical side of the distinctive character of a municipality:

Under the bankruptcy law, a municipal bankruptcy is the bankruptcy of a city, town, or other state subdivision, or public agency or instrumentality of a state (such as a school district or sanitary district). A municipality is different from other debtors who file bankruptcy, because, unlike other debtors, a municipality cannot simply go out of business. It must continue to provide its residents with essential services such as police protection, fire protection, sewage and garbage removal, and schools. Thus, chapter 9 of the Bankruptcy Code (11 U.S.C. 901 et. seq.) is designed just for municipalities, to keep them in existence by allowing municipalities to adjust their debts (11 U.S.C. 941).

H.R. Rep. No. 1011, 100th Cong., 2d Sess. 2 (1988). See also 134 Cong. Rec. H9302 (daily ed. Oct. 3, 1988) (statement of Rep. Rodino); 134 Cong. Rec. H10407 (daily ed. Oct. 19, 1988) (statement of Rep. Edwards).

The specific amendment to the Bankruptcy Code addressed by this question reflects the special nature of municipal bankruptcies. Indeed the language of the provision in question is

significantly different from that now proposed by S.46 in that it required "any regulatory or electoral approval necessary under applicable nonbankruptcy law." Municipal Bankruptcy Amendments, Pub. L. No. 100-597, § 10(3), 102 Stat. 3028, 3030 (1988) (emphasis added). Other changes reflected the unique methods by which a municipality funds its operations. E.g., Municipal Bankruptcy Amendments, supra, §§ 4(2), 7(2), 102 Stat. 3028, 3029 (limitations on recourse to special revenues). See also S. Rep. No. 506, supra, at 4 ("application of commercial law concepts to municipal corporations runs afoul of the traditional structure of revenue bond finance"); id., at 9 ("[I]f water revenues are insufficient to pay operating expenses and the debt service on water revenue bonds, other funds of the city should not be reachable to pay the bonds."); H.R. Rep. No. 1011, supra, at 4 (explaining that operation of the Bankruptcy Code without special provisions for municipalities might run afoul of state constitutions by in effect turning special revenue bonds into general obligation bonds, "but without the authorization by popular vote usually required before a municipality can issue a general obligation bond").

Thus, though the end goal of a municipal bankruptcy may be similar to that of a Chapter 11 reorganization, the route a bankruptcy proceeding must follow to achieve that goal is decidedly different, due to the constitutional and practical consequences of the governmental character of a bankrupt municipality.

It is also important to recognize that the rationale of the Municipal Bankruptcy Amendments and of S.46 are markedly different. The 1988 Act sought to change the law to assist what many saw as the plight of a specific class of bankrupt entities, municipalities. That Act was, as I testified before the House Judiciary Subcommittee on Monopolies and Commercial Law in 1988, designed to avoid the serious problems the original Chapter 9 could have caused a bankrupt municipality in working out its debt adjustment. Legislation to Amend Chapter 9 of the Bankruptcy Code: Hearings Before the Subcomm. on Monopolies and Commercial Law of the House Comm. on the Judiciary, 100th Cong., 2d Sess. 22 (1988) (testimony of Richard Levin). Indeed, even outside the context of an actual bankruptcy, the old provisions of chapter 9 had very troubling implications for the municipal finance market. See H.R. Rep. No. 1011, supra, at 5.

S.46, in contrast, is not designed to assist the expeditious return of a failing utility to economic vitality. Rather, this bill serves to change the law in a particular case merely to expand the jurisdiction of state nonbankruptcy regulatory authorities. Moreover, if S.46 builds upon the Chapter 9 provision then it clearly constitutes a change in the law that should not be made retroactive.

QUESTION SUBMITTED BY SENATOR GRASSLEY

1. THE ATTORNEY GENERAL ARGUES THAT WITHOUT THIS BILL, PSNH INVESTORS WILL ENJOY A WINDFALL OF PROFITS, ALL COURTESY OF NEW HAMPSHIRE RATEPAYERS. HE SAYS THIS IS ESPECIALLY UNFAIR, SINCE THESE INVESTORS KNEW THEY WERE TAKING THE RISK OF CONSTRUCTION OF SEABROOK. WHAT IS YOUR RESPONSE?

ANSWER

S.46 is designed to block the potential restructuring of the Public Service Company of New Hampshire as proposed in the original plan of reorganization submitted by Public Service. Under that plan, Public Service would be reshaped into a holding company structure, including a subsidiary engaged in the wholesale sales of electric power. The rates for those sales would be regulated by the Federal Energy Regulatory Commission ("FERC"). FERC, like the majority of states, but unlike New Hampshire, allows rates to include some return on construction work in progress ("CWIP") before a new plant is commercially producing power. Presumably, it is this partial return on CWIP that the Attorney General characterizes as a "windfall profit," and blocking such a return is the target of S.46.

The short answer to this question is that events have now progressed to the point that there cannot realistically be the kind of "windfall profits" about which the Attorney General complains, whether or not S.46 is enacted into law. By all informed evaluations, including that of the outgoing chairman of the New

Hampshire Public Utilities Commission ("NHPUC"), and even Sen. Rudman, Seabrook is likely to begin commercial operations in early 1990. At that point, there is no "construction work in progress," and Public Service is by law entitled to a full and fair return on capital prudently invested in Seabrook. (Independent auditors hired by the NHPUC reported that, in their view, 93% of Seabrook investment was prudent.)

In other words, the "risk of construction" noted in this question has paid off (or will very soon) in the form of a working power plant. The ratepayers of New Hampshire have benefited from the money investors were willing to tie up in the long construction of Seabrook -- a vitally needed power source that would not have been built without that money. The ratepayers will soon benefit from the electricity generated by Seabrook. At long last paying Seabrook investors a return on their investment is hardly a "windfall" for them by any measure.

Moreover, the law governing ratemaking -- which applies whether or not a utility is in bankruptcy -- allocates risk to protect both ratepayers and investors. Under that body of law, a utility is entitled to a fair return on all capital prudently invested in a used and useful plant. If a utility makes an investment decision that is imprudent based on the information reasonably available to it at the time of its decision, all costs associated with that decision are disallowed in determining the

rates a utility can charge. If the investment was prudent, the utility may receive a return on it through rates, but at most that return is a regulated rate of return. In this case, Public Service will have to write off well over \$1 billion of its Seabrook investment. And if Seabrook does not operate and S.46 passes, Public Service will have to write off even the nearly \$700 million of its Seabrook investment that was made before the 1979 enactment of New Hampshire's anti-CWIP law. In sum, with or without S.46, there are simply no "windfall profits" possible for Public Service.

QUESTIONS SUBMITTED BY SENATOR THURMOND

1. MR. LEVIN, IN YOUR PREPARED STATEMENT YOU MENTION YOUR PARTICIPATION AS COUNSEL TO THE HOUSE SUBCOMMITTEE WHICH WORKED ON WHAT BECAME THE BANKRUPTCY REFORM ACT OF 1978. S.46 CONTEMPLATES A RETURN TO GREATER AGENCY INVOLVEMENT IN THE BANKRUPTCY PROCESS AND PROCEDURE. BASED UPON YOUR EXPERIENCE WITH THE BANKRUPTCY REFORM ACT OF 1978, COULD YOU INFORM THIS SUBCOMMITTEE AS TO THE POLICY RATIONALE FOR EXCLUDING AGENCY PARTICIPATION IN THE CONFIRMATION OF REORGANIZATION PLANS?

ANSWER

In 1978, Congress repealed the veto power of nonbankruptcy agencies -- both state and federal -- over reorganization plans that S.46 now seeks to recreate. At that time, no central institution controlled the reorganization process, and that process was burdened by multiple levels of bureaucratic review and the unwarranted and costly delays that entailed. A reorganization plan could be stymied by inconsistent or conflicting rulings of different agencies claiming jurisdiction; one agency might approve the transaction while the other disapproved it, or two agencies might place inconsistent conditions on their approval of the transaction. Certainly only those who benefited from extended legal proceedings themselves -- as opposed to those who stood to benefit from a reorganized and rejuvenated company -- benefited from this cumbersome process, a process S.46 seeks to revive.

By 1978, it had become clear to Congress that the extent of the authority it had given to both federal and state nonbankruptcy regulators to review or approve reorganization plans was counterproductive. As my review of the legislative history of the Bankruptcy Code in my prepared statement makes clear, in 1978 Congress determined that the delays involved in requiring multiple determinations on the merits of proposed plans, i.e., of both a regulatory agency (or agencies) and the bankruptcy court, were unnecessary, and that the bankruptcy court was not only fully capable of resolving the competing interests presented in a reorganization case, but also the best, neutral forum for doing so. It made sense to allow regulatory agencies to advocate their views regarding particular plans before the bankruptcy court, but not to control the plan outcome. Where federal and state regulatory agencies possess a special expertise that is not also within the province of the bankruptcy court -- ratemaking -- Congress left their authority undisturbed.

Removing the veto power of non-bankruptcy agencies also put their role in the reorganization process in proper perspective. For though such agencies serve a public interest, theirs is a focused mission and a discrete expertise. These agencies are simply not suited to the broad scale resolution of various public and private interests demanded in reorganization proceedings. Indeed, Congress did not appear willing to adopt the view that a nonbankruptcy agency, whether state or federal, as the advocate

of a particular public interest, was the right entity to conduct an impartial balancing of all public interests and the rights and interests of the creditors and shareholders involved in a reorganization. Moreover, giving a politically independent bankruptcy court control over the plan adjudicatory process helps insulate that process from the adverse influence of the political and special interests with which nonbankruptcy regulators must deal.

2. MR. LEVIN, AS COUNSEL TO THE PUBLIC SERVICE COMPANY OF NEW HAMPSHIRE, COULD YOU EXPLAIN TO THE SUBCOMMITTEE THE CONSEQUENCES OF SETTING UP A HOLDING COMPANY? WHAT PRACTICAL EFFECT, IF ANY, WILL THIS HAVE ON THE REGULATION OF UTILITY RATES IF LEGISLATION SUCH AS S.46 IS NOT ENACTED?

ANSWER

The original plan of reorganization submitted by Public Service Company of New Hampshire proposed that Public Service's primary business of producing, transmitting and distributing electricity and services related thereto, be grouped into separate, but affiliated companies, held by a common holding company. Such a restructuring served several purposes. One primary purpose was to place the regulation of electric rates for wholesale services entirely before the Federal Energy Regulatory Commission ("FERC"). Placing wholesale production and transmission rates under FERC regulation would enable the restructured companies to recover over time a certain amount of Seabrook-related costs before Seabrook was in commercial operation. Virtually all utilities other than Public Service which serve retail customers in New Hampshire receive power under FERC-regulated rates.

The restructuring proposed under the original plan was also intended to more readily allow the restructured companies to participate in, or develop power from, independent sources and provide competitive services to other New Hampshire utilities. To that end, additional subsidiaries might be formed. An additional effect of the restructuring as originally proposed would make it

possible to form additional subsidiaries to carry on non-utility businesses in the event it was desirable in the future to pursue such diversification.

Notwithstanding the partial jurisdiction of FERC in a holding company structure, under New Hampshire law the state public utilities commission remains the ultimate gatekeeper to the marketplace, as has been explained by the New Hampshire Supreme Court relatively recently in In re Sinclair Machine Products, Inc., 126 N.H. 822, 498 A.2d 696 (1985). In Sinclair, a utility providing retail service in New Hampshire bought most of its power at wholesale from its parent company. The rate charged by the wholesaler was approved by FERC and, under FERC's regulations, properly included some return on investment in two abandoned power plants. This return would have been prohibited if the wholesale transaction had been within the jurisdiction of the New Hampshire Public Utilities Commissions ("NHPUC"). The issue in the case was what role the NHPUC could play in approving the retail rate ultimately charged by the retailer, in light of FERC's approval of the wholesale rate.

The NHPUC held that FERC's approval of the wholesale rate preempted it from examining that rate as a cost to the retailer, and so required that the cost of the wholesale purchase be passed on to the retailer's customers as a reasonable expense of doing

business. However, the New Hampshire Supreme Court reversed this ruling by the NHPUC and remanded for further proceedings.

The Court quite clearly stated:

We hold that federal preemption of State authority requires that the wholesale rate fixed by the FERC binds the PUC, to the extent that the PUC may not disapprove such a rate even in light of the State's anti-CWIP statute. However, the PUC may always inquire into the reasonableness of a utility's purchasing power under a FERC-approved rate given other purchase options available to the utility.

498 A.2d at 699 (emphasis added). The Court went on to elaborate:

The PUC correctly determined under federal preemption principles that FERC approval of a wholesale rate precludes the PUC from questioning the reasonableness of that charge. However, it does not follow automatically that the PUC must find that power costs incurred under a wholesale rate are necessarily a reasonable expense for the retailer.

Id. (emphases in original). "Thus," the Court concluded, "the PUC is not preempted from determining the reasonableness or prudence of [the retailer's] initial purchase of [the wholesaler's] power or its continued participation under this rate schedule." Id. at 705.

In sum, the language of Sinclair makes clear that the NHPUC has a role in regulating the retailer's ability to pass wholesale rates through to retail customers. Furthermore, that role is not

limited merely to approving a wholesale contract as prudent in the first instance, because, as the court clearly states, the retailer's "continued participation" in the contract is also within the NHPUC's purview.

Of course, as I pointed out in my prepared statement, the issue of receiving a return on the investment in Seabrook before that plant was in commercial operation has largely disappeared from this case as a practical matter because Seabrook is likely to come on-line in early 1990. Thus the need to create a FERC--regulated holding company to permit pre-operational inclusion in rates of a portion of the Seabrook investment has greatly diminished.

In terms of the impact of the Seabrook investment on rates, the holding company structure would have little overall impact on the ultimate level of rates. A utility is entitled to a fair and reasonable return on all capital prudently invested in a plant. New Hampshire law essentially prohibits such a return until a new plant is in commercial operation, while FERC regulations allow some return on that investment while it is under construction. The impact of the holding company structure in the present circumstances of the Public Service case, then, is basically one of timing -- a return on Seabrook would be allowed before it was operating commercially. Once commercial operation occurs, rates must produce a fair return on the prudent investment in Seabrook.

whether or not Public Service has been reorganized into a holding company structure.

It should also be remembered that, if the control of rates is the central concern of the proponents of S.46, this bill employs an axe where a scalpel will do. For though it is through corporate restructuring, in this particular instance, that Public Service would have secured FERC jurisdiction over part of its rates, the design of Chapter 11 does not need to be disrupted in order to preserve state control over rates. An explicit provision -- amending either the Bankruptcy Code or the Federal Power Act -- to give state commissions the specific authority to review FERC-established rates would more directly achieve this end. Of course, such an amendment raises its own questions, but they are more precisely related to the motivating concerns of the sponsors of S.46 than are the blunderbuss provisions of this bill.

In summary, the holding company structure originally proposed by Public Service would have had an effect on the timing of the impact of Seabrook on rates. However, events have overtaken the original reorganization plan, and it is far from clear whether the holding company structure remains an attractive or necessary option. Given the current state of negotiations and the proposals before the bankruptcy court, it appears unlikely, though not completely impossible, that Public Service will come out of its reorganization proceedings as a FERC-regulated holding company.

3. MR. LEVIN, IN YOUR OPINION, IS THERE ANYTHING FUNDAMENTALLY UNIQUE ABOUT A UTILITY REORGANIZATION THAT WOULD WARRANT THE SPECIAL TREATMENT AFFORDED BY S.46? .

ANSWER

No. There are unique things about a utility reorganization, but not things that would warrant a departure from the broad general principles of reorganization law. As my prepared statement explains, Congress adopted a broad deregulatory policy in its revision of reorganization procedures in 1978, focusing control over those proceedings in the bankruptcy court. The veto power of the federal non-bankruptcy agencies -- such as the Interstate Commerce Commission and the Securities and Exchange Commission -- was eliminated, as well as that of state regulators. All the arguments to expand the authority of a state public utilities commission made here could equally be applied to the authority of any non-bankruptcy regulator. This bill thus is an invitation to revisit the fundamental approach of the whole 1978 revision of the bankruptcy laws. Those issues were fully considered in 1978. Congress should not undo the careful compromises reached after nearly a decade of study, simply to dictate the outcome of a single case by retroactive legislation.

Senator HEFLIN. You indicated that when Congress revised the Bankruptcy Code in 1978 that Congress intended to reduce the regulatory control over the confirmation of a reorganization plan.

Mr. LEVIN. Yes.

Senator HEFLIN. But the language you are relying upon in section 1123(a), which is "notwithstanding any other applicable non-bankruptcy law," was added in the 1984 amendments. What do you offer as evidence that Congress intended to preempt State regulatory laws?

Mr. LEVIN. There is language in the Senate and House committee reports from 1978 regarding section 1123. I think you have the report numbers, although I could give them to you, that the section 1123 was designed to preempt State law. There is statements on the floor, statements which are cited in my prepared statement, and most importantly, something that is not cited that I want to call to your attention today. In 1979 and 1980 when the first draft of the technical amendments bill came out, it ultimately was enacted in 1984, the very first House version of that bill, not the Senate version, but the House version contained the notwithstanding law. It was developed in early 1980, and the House report accompanying that is much more expansive than later reports describing that provision.

Later reports say this is technical, stylistic change. The House report then, and I do not have the report number with me—I can provide it to staff later—says something like this amendment is intended to make clear that the section 1123 dictates, and in effect, preempts what can be done in a reorganization plan. I do not have the exact words here, but the language can be found in House Report 96-1195 (1980).

Senator HEFLIN. All right.

Well, if, in fact, your interpretation of 1123(a) is correct, what is to prevent utility companies from filing chapter 11 petitions to circumvent the State regulatory process?

Mr. LEVIN. That is an argument that is often heard in bankruptcy cases. What is to prevent them is the difficulty and enormous problems that arise from bankruptcy cases. It is my experience in 3 years working on the House side and in 13 years of practicing or 11 years of practicing bankruptcy law since then, the last thing any company wants to do is run into the bankruptcy court.

This company in particular, even with this prospect, resisted at every opportunity. It could have filed for bankruptcy in 1984 when its first liquidity crisis hit, and after which the bonds referred to earlier were issued. Companies do not run willy-nilly into bankruptcy. Even the megacases that receive so much press are not cases of solvent companies. They are cases with real cash flow problems, real debt problems, other kinds of problems that cannot be addressed outside of an adjustment with creditors or other parties with whom they have contracts.

Senator HEFLIN. There is a concern that by allowing Public Service to reorganize as a holding company partly under FERC's jurisdiction, the burden of financing the Seabrook plant is shifted from the stockholders to the ratepayers. How do you respond to this concern?

Mr. LEVIN. That is a concern that might have some applicability if Seabrook were not operational. The anti-CWIP law says the stockholders must take that risk. Once Seabrook becomes operational, it becomes up to the ratepayers, and I might point out, Mr. Chairman—this is important—even under the plan that was filed in December by Public Service Co., that company was writing off, was proposing to write off under that plan close to \$1 billion of its investment, not to charge ratepayers for \$1 billion.

It is hard to listen to the proponents of the legislation say that the entire risk of the investment is being placed on the ratepayers when there is that kind of writeoff contemplated in that plan.

Senator HEFLIN. We will submit some other questions to you in writing. We would appreciate your prompt response.

Mr. LEVIN. Thank you, Mr. Chairman.

Senator HEFLIN. Senator Thurmond, do you have questions?

Senator THURMOND. Mr. Levin, has not this matter boiled down to whether the State utility commissions are going to fix rates or whether some government agency might fix rates? In other words, if you pass this bill, then the utility commission in New Hampshire will fix rates, and under the law, they have to allow such rates so that a company can survive and make a fair profit, a reasonable profit.

Mr. LEVIN. Senator, if that is the issue—

Senator THURMOND. If this bill passes. Now what is wrong with that?

Mr. LEVIN. Senator, if that is the issue your earlier question to the prior panel is exactly the right question: why is this a bankruptcy issue. If that is the issue, then the statements of the management, both in court and in the public—in the Public Service case, Public Service was not actively pursuing the holding company plan, but was rather pursuing negotiations with the State over reasonable rates—have been totally disregarded. This, the plan that was filed in December is one possibility. It is not an all or nothing possibility.

Public Service is in very active negotiations with the assistance of a court-appointed examiner over the rate issue with the State of New Hampshire, and there is by no means any certainty that even if this bill is not enacted that Public Service will follow the holding company plan route proposed in December.

Senator THURMOND. Now if this bill does not pass, then the FERC could come in and fix rates; you admit that, do you not?

Mr. LEVIN. Well, as I said, it depends whether rate negotiations with the State of New Hampshire are successful.

Senator THURMOND. I say they could do it; they could do it?

Mr. LEVIN. It could. It is possible, but not unilaterally. Public Service would have to move in that direction.

Senator THURMOND. Well, now if this bill passes, then the rates will be determined by the utility commission in New Hampshire, and under the law they have to allow a rate that will enable the company to survive and make a reasonable profit.

Mr. LEVIN. That is correct.

Senator THURMOND. So what is the objection to passing this bill and keeping the rates in New Hampshire? Why not let the States control rates?

Mr. LEVIN. Well, as I said——

Senator THURMOND. Should we do nothing and then allow the Federal agency to come into this matter and fix rates when the States can do it and have to do it in order to allow companies to survive?

Mr. LEVIN. There are a couple of answers, Senator. As I said, the agency that sets rates does not matter so much once Seabrook becomes operational because the anti-CWIP law that prevents Public Service from recovering any of its Seabrook investment no longer applies. It only applies until that plan becomes operational, and at that point you are correct. The New Hampshire PUC has the responsibility to set just and reasonable rates.

So in that sense, and now that it seems that Seabrook's operation is assured, the focus in the case has been on getting an adequate return from the New Hampshire PUC, not from the Federal Energy Regulatory Commission.

Senator THURMOND. Well, they would have to get an adequate return. Under the law they would have to in New Hampshire. If you pass this bill, they will still have to do that. I am in favor of nuclear power. I am in favor of Seabrook plant. I do not hesitate to say that. On the other hand, I hesitate to shift power from the States to the Federal Government. We have been doing that for years and years. We have done too much of that.

And why not let the States continue to control these rates because under the law, they have to give a reasonable profit to the company to survive and pay them a fair profit.

Mr. LEVIN. Senator, there is a lot of merit in what you say. The problem, I think, is that the State's representatives forgot a leading New Hampshire case that says that the State can do exactly what these representatives said it cannot do, and that is control rates that are set by FERC on the pass to the retail level. And that is the Sinclair Machine case. I do not have a cite with me. But it specifically says that if the retail company is imprudent in buying under that wholesale contract, the State utility commission has the authority to cut those rates to the retail customer.

Senator THURMOND. Mr. Chairman, that is all I have.

Senator HEFLIN. Thank you.

Mr. LEVIN. Thank you, Mr. Chairman.

Senator HEFLIN. We will call the remaining witnesses as a panel of four: Mr. James Monk, chairman of the Indiana Utility Regulatory Commission; Mr. Dan Borson, energy policy analyst, Public Citizen; Roger Whelan, from Washington, P.C. member of the American Bankruptcy Institute; and Leonard M. Rosen, from New York, the chairman of the National Bankruptcy Conference.

If you will, your full written statements will be made part of the record. Please summarize in less than 5 minutes. Mr. Monk, please proceed.

PANEL CONSISTING OF JAMES MONK, CHAIRMAN, INDIANA UTILITY REGULATORY COMMISSION, INDIANAPOLIS, IN; DAN BORSON, ENERGY POLICY ANALYST, PUBLIC CITIZEN, WASHINGTON, DC; HON. ROGER WHELAN, WASHINGTON, DC, MEMBER, AMERICAN BANKRUPTCY INSTITUTE; AND LEONARD M. ROSEN, NEW YORK, NY, CHAIRMAN, NATIONAL BANKRUPTCY CONFERENCE

STATEMENT OF JAMES MONK

Mr. MONK. Thank you, Mr. Chairman, Senator Thurmond. It is an honor to be with you today and to present to you the perspective of a State utility regulator. The Indiana Utility Regulatory Commission is fully supportive of Senate bill 46. Unfortunately, in Indiana we have had some experience with situations which are similar to the one which apparently is the genesis of this particular bill. We have had two failed nuclear construction projects in Indiana: Northern Indiana Public Service Co. had a project which did not get very far down the road, and they were able to pull out of that without too much financial difficulty.

On the other hand, Public Service Indiana, our State's largest utility, tried to build a nuclear power plant called Marble Hill, and got so far into the project that at the time it was canceled in 1985, they were essentially on the verge of bankruptcy. Our State commission at that time took action rather than let Public Service Indiana go into bankruptcy, took action in the form of an emergency rate relief procedure and essentially was able to avoid Public Service Indiana going into bankruptcy.

I think there is some lesson to be learned there in that State utility regulators can, in fact, handle situations such as this, as we have done in Indiana. With Public Service Indiana we have now rolled back the emergency rate relief that was granted in 1985, and in October of this year, the rates that Public Service Indiana charges will be back to the 1985 level. The company is now financially stable, and in fact, we are very pleased with the whole situation the way this all turned out.

And it was basically done by State regulators through the existing regulatory process and without the interference and/or quote "assistance" of the bankruptcy court. We feel on two levels that the State regulatory commissions are the proper jurisdiction, the proper forum for these types of matters, and not the bankruptcy court. One of those is a constitutional level. The other one is a very practical level in that we are charged with the responsibility of balancing the various interests which are in question: the interests of the ratepayer, the interest of the investors, and the interest of the stockholders. And we do that on a daily basis.

We have experience and are adept at it. There are 75 years of law and tradition in the State regulatory commissions which show that we can do that job in addition to some of the recent experiences. And we feel that rather than have the very limited perspective that a bankruptcy court might have when dealing with what is a very unique entity, that is a public utility, which is highly regulated, which if negatively affected can not only have an effect on the company but also could have an effect on the economy of the

State and in terms of electric utilities maybe even on the health and safety of the citizenry.

We feel that those issues are best left to those of us in the regulatory arena who deal with them on a daily basis, and for that reason we would be supportive of Senate bill 46. And we thank you.

[The statement of Mr. Monk and answers to questions submitted by Senators Heflin and Thurmond follow:]

STATEMENT OF JAMES R. MONK, CHAIRMAN
INDIANA UTILITY REGULATORY COMMISSION
SENATE SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE
July 26, 1989

The Indiana Utility Regulatory Commission, which is charged by Indiana statute with regulation of electric utilities and other types of utilities in the State of Indiana, supports the passage of Senate Bill 46.

Unfortunately, in Indiana we have had considerable experience regarding bankrupt or potentially bankrupt electric utilities. Due to the unsuccessful construction of the Marble Hill Nuclear Power Plant, Public Service Company of Indiana, our largest utility, was on the verge of bankruptcy in 1985. In March, 1986, our Commission granted Public Service Indiana an emergency rate increase to save PSI from bankruptcy. One of the reasons that this Commission determined it to be essential that PSI not become bankrupt is the very problem addressed by Senate Bill 46: that is the extent to which a bankruptcy court might attempt to set rates for a utility's electric customers contrary to the orders of the State's legitimate ratemaking agency. As with the present situation in the State of New Hampshire, our Commission feared that in order to satisfy the demands of creditors, a bankruptcy court would excessively raise the rates of utility customers. *WVPA is now in bankruptcy*

As has been the tradition and law in the United States for three quarters of a century, we believe that the appropriate jurisdiction for setting retail rates of electric utilities is the state public utility commissions. State utility commissions

are experienced and adept at balancing the interests of investors and stockholders with ratepayers. We believe that a bankruptcy court might give an unfair advantage to creditors and that ratepayers might not be given proper consideration and/or protection in such proceedings.

It is important to note that utilities are unique and should not be treated in the same manner as other private corporations. Utilities provide essential public service, a fact which has been recognized by both Federal and State law in giving utilities unique status and privileges in exchange for regulation by appropriate federal and state agencies. Because electric utilities are regulated monopolies, ratepayers can only be properly protected by duly constituted regulatory authorities. In a bankruptcy proceeding our Commission fears that ratepayers may become captive providers of capital to be divided up among insistent creditors. A public utility provides essential public services and, thus, cannot be allowed to go out of business. Service must continue to be provided to the customers. This is not the case with other entities that come before Federal Bankruptcy Courts. In the case of electric utilities not only is the economy within the service territory of the particular utility at risk when such a utility goes bankrupt, but also in jeopardy is the very health and safety of the citizens. Therefore, it seems clear to our Commission that a bankruptcy court is not the proper jurisdiction to consider these issues. It is equally obvious that the proper forum for review of such issues is the state public utility commission.

We believe that this proposed legislation presents a basic question of States' rights and that the very foundation of traditional jurisdiction over retail electric rates of public utilities is at stake in this debate. In a recent decision dated May 16, 1989, in the United States District Court for the Southern District of Indiana in a case involving the authority of the Rural Electrification Administration to dictate the rates of Wabash Valley Power Association, Inc., the Court said,

"the action of the United States Rural Electrification Administration in, by letter, asserting ratemaking jurisdiction over Wabash Valley Power Association, Inc. usurping the ratemaking authority of the Indiana Utility Regulatory Commission and the Michigan Public Service Commission, and purporting unilaterally to set Wabash Valley Power Association's wholesale rates is arbitrary, capricious, and not in accordance with law."

Our Commission views this decision as an important step in upholding the right of a State, rather than the Federal Government, to regulate the electric rates of Wabash Valley Power and other public utilities. We believe it is crucial that the right of a State to protect its own citizenry in terms of the setting of fair and equitable retail electric utility rates be upheld and therefore we strongly urge passage of Senate Bill 46 believing that said passage will give statutory protection to that right.

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION
913 STATE OFFICE BUILDING



INDIANAPOLIS 46204-2284

August 23, 1989

The Honorable Howell Heflin
United States Senate
Subcommittee on Courts and Administrative Practice
Senate Judiciary Committee
223 Hart Senate Office Building
Washington, D.C. 20510

Dear Senator Heflin:

Thank you for your kind letter of August 3, 1989, regarding my testimony before your Subcommittee on S. 46, the "Electric Utility Bankruptcy Clarification Act."

Attached please find a memorandum prepared by our Commission staff in answer to the additional written questions which you and Senator Thurmond posed by way of the above-referenced letter. I hope these responses are helpful to you and the other members of the Subcommittee in your consideration of S. 46.

Please advise if further information is required in this regard. Again, thank you for your cooperation and consideration.

Yours truly,

A handwritten signature in dark ink, appearing to read "James R. Monk".

James R. Monk
Chairman

JRM:cc

Enclosure

STATE OF INDIANA



INDIANAPOLIS, 46204-2284

INDIANA UTILITY REGULATORY COMMISSION
913 STATE OFFICE BUILDING

MEMORANDUM

TO: ROBERT C. GLAZIER, UTILITIES DIRECTOR

FROM: EDWARD K. PHELAN, CHIEF ECONOMIST *EKP*

RE: U.S. SENATE QUESTIONNAIRE ON THE PROPOSED "ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT," S.46 -- AMENDED RESPONSE

DATE: AUGUST 18, 1989

Pursuant to your request of August 14, 1989, and your subsequent instructions of August 17, 1989, we are resubmitting a series of answers to the questions forwarded by Senators Heflin and Thurmond to Commission Chairman Monk, following the Chairman's testimony on S.46 before the Subcommittee on Courts and Administrative Practice of the Judiciary Committee, U.S. Senate. Our answers generally reflect our current knowledge about the requested information, and they have been drafted on the basis of a moderate research effort. If detailed responses were to be required, we would have to devote substantially greater efforts for in-depth research and documentation. The present memorandum amends our August 16, 1989 response to your original request. The responses to the U.S. Senate questionnaire are contained in the Attachment.

EKP/LEP/lep

Attachment

NBI DOC ID: FLP/UTILBANKRI

ATTACHMENT
Page 1 of 6

A. QUESTIONS OF SENATOR HEFLIN

1. Utility Bankruptcies in Other States

Public Service of New Hampshire (PSNH) has been the only investor-owned electric utility that formally declared bankruptcy in recent years. As the testimony of Chairman Monk indicated, Public Service Company of Indiana (PSI) was rescued from a bankruptcy. Similar situations have developed with Long Island Lighting Company (LILCO) in the state of New York as a result of the Shoreham nuclear project, and with Consumers Power Company (Consumers Power) in Michigan as a result of the Midland nuclear project. Formal declarations of bankruptcy, however, have occurred with higher frequency among electric cooperatives. Similarly, the Rural Electrification Administration (REA) has been engaged in numerous debt restructuring efforts for electric cooperatives that are near or technically in bankruptcy. Of course, the bankruptcy of the Washington Public Power Supply System should continue to be in our minds.

There is a general familiarity with the events leading to the declaration of bankruptcy by the Wabash Valley Power Association (WVPA) in Indiana. The January 1984 abandonment of PSI's Marble Hill nuclear project in which WVPA held a 17% interest, led WVPA to default on approximately \$500 million of REA guaranteed loans in November 1984, and to seek Chapter 11 bankruptcy protection in May 1985 (the total WVPA debt to REA for various construction projects, including Marble Hill, was \$622 million at the end of 1984). WVPA, with the encouragement of the REA, petitioned the Indiana Commission for a 51% rate increase in April 1984. That petition was stayed and it was eventually dismissed in January 1987, on the grounds that the rate increase would have been used for the recovery of costs associated with a utility investment that was not "used and useful" (the Indiana Supreme Court had held in 1985 that the costs associated with abandoned utility investments could not be recovered from utility ratepayers; see discussion on "anti-CWIP" statutes, *infra*). The REA appealed the 1987 decision of the Indiana Commission to the Indiana Court of Appeals, which, however, upheld the Commission's Order. National Rural Util. Coop. Fin. Corp. v. Public Serv. Comm'n, 528 N.E.2d 95 (Ind. App. 1988), cited and discussed in Wabash Valley Power Ass'n v. Rural Electrification Admin., No. IP 89-126-C, slip op. at 2, 3 (S.D. Ind. 1989). By letter communications dated November 23, 1988, the REA informed WVPA, the Indiana Utility Regulatory Commission and the Michigan Public Service Commission, that it would exercise jurisdiction "over the rates charged by Wabash." WVPA initiated an action for a "declaratory judgment that REA lacks the authority to usurp state ratemaking authority by letter and unilaterally regulate Wabash's wholesale rates." Wabash Valley Power Ass'n v. Rural Electrification Admin., *supra*, at 3. On May 16, 1989, the United States District Court for the Southern District of Indiana issued a declaratory judgment finding that REA's assertion of "ratemaking jurisdiction over Wabash Valley Power Association, Inc., usurping the ratemaking authority of the Indiana Utility Regulatory Commission and the Michigan Public Service Commission, and undertaking to dictate Wabash's wholesale rates [was] arbitrary, capricious, not in accordance with law, and of no force and effect whatever." The currently outstanding REA debt associated with WVPA's involvement in the cancelled Marble Hill nuclear project amounts to \$728 million, of which WVPA recognizes \$683 million in its financial statements (WVPA Annual Report to the Commission, "Notes to Financial Statements," p. 3).

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On June 5, 1989, certain creditor banks filed a petition for involuntary bankruptcy against the Colorado-Ute Electric Association, Inc (Colorado-Ute). According to information from the Colorado Public Utilities Commission this cooperative has debts of \$262.9 million to the National Rural Utilities Cooperative Finance Corporation (CFC) and of \$425.4 million to the Federal Financing Bank (FFB), which are guaranteed by the REA. On March 30, 1989 Colorado-UTE elected not to make a \$12.6 million payment on CFC and FFB loans, thus technically defaulting on its U.S. obligations (E. Andrews, "Colorado-Ute's workout plan," Standard & Poor's Creditweek, May 8, 1989, p. 18). The U.S. Department of Justice permitted Colorado-Ute to make a timely \$21 million payment on its \$223 million leveraged lease debt on July 3, 1989, whereby the cooperative has avoided default on that debt, and has negotiated a standstill agreement with its creditors. Colorado-Ute has also received proposals for the purchase of its generation and transmission assets from other cooperative and investor-owned utilities (C. Ruppert, J. Costagliola, "Colorado-Ute avoids default, attracts bidders," Standard & Poor's Creditweek, July 10, 1989, p. 17). The situation of Colorado-Ute is a result of excess generating capacity which was installed in anticipation of power demand from its member cooperatives that did not materialize (lack of oil shale exploitation). Colorado-Ute has 1,200 MW of capacity with an 800 MW peak demand, and a 460 MW average usage demand. The cooperative has implemented an 8% rate increase which is subject to review by the Colorado PUC. Due to its operating losses, Colorado-Ute has been obliged to borrow heavily in order to finance its operations (the cooperative has incurred \$29 million of "negative equity," and has issued \$25 million of commercial paper). The Colorado PUC is maintaining jurisdiction over the cooperative's revenue requirement.

On August 31, 1987 the Eastern Maine Electric Cooperative, Inc. (Eastern Maine) filed for Chapter 11 bankruptcy protection due to its involvement with PSNH's Seabrook nuclear project. At that time Eastern Maine was providing service to 9,400 rural customers and had total liabilities of \$32.4 million which included \$11.1 million of REA debt (D. Wessel, "Tiny Utility Files Under Chapter 11 Blames 'Financial Burden' of Seabrook," The Wall Street Journal, September 1, 1987, p. 37). The REA is currently engaged in debt restructuring negotiations with three other electric cooperatives in New Hampshire and Vermont that are also involved in the PSNH Seabrook nuclear project but have not entered Chapter 11 proceedings (New Hampshire Electric Cooperative, Vermont Electric Cooperative and Vermont G&T Cooperative).

The REA has entered into numerous debt restructuring agreements with troubled electric cooperatives and is actively negotiating such agreements with a number of cooperatives. The Kansas Corporation Commission in 1985 had denied such an agreement between the Sunflower Power Cooperative, the REA and CFC, because it contained provisions for partial debt forgiveness in exchange for an immediate \$2 million rate increase. The Kansas CC approved in 1986 a subsequent debt restructuring agreement for Sunflower which did not involve any rate increases. The cooperative had not filed for Chapter 11 bankruptcy protection, but it was in technical default on its REA and CFC obligations. The Kansas CC has maintained jurisdiction over the cooperative's rates. In Kentucky, the Big Rivers Electric Corporation was also faced with the issues of excess generating capacity and REA debt restructuring. The Big Rivers construction of the Wilson Units 1 and 2 had received prior approval by the Kentucky Public Service Commission in June 1980. Changes in the power demand of aluminum smelters led to the cancellation of Wilson Unit 2 in April 1981. In

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1984 the REA refused to advance any additional committed loan funds for the completion of Wilson Unit 1, and in order to complete the Unit Big Rivers used internally generated funds and stopped payments on its REA debt. The REA and the U.S. Department of Justice filed a foreclosure suit against Big Rivers in January 1985 seeking to recover \$1.1 billion of indebtedness. In August 1986, Big Rivers petitioned the Kentucky PSC for an actual \$22.9 million rate increase (11%), and for approval of a debt restructuring plan that was requiring additional rate increases in 1989 and 1991 (In re Big Rivers Electric Corp., (Ken. PSC March 17, 1987) Case No. 9613). The Kentucky PSC initially rejected both the rate increase request and the debt restructuring plan. The Kentucky PSC, however, later approved a "phase one increase of 15 million dollars," accepted the notion of "cooperative federalism" with the REA, adopted a new debt restructuring plan (the "workout plan"), and tied the Big Rivers' rates for the aluminum smelters to the price of aluminum (In re Big Rivers Electric Corp. (Ken. PSC August 10, 1987) Case No. 9885, 89 P.U.R.4th 499 (1988)). The Kentucky PSC's actions were premised on the dismissal of the federal lawsuits against Big Rivers, and on the lifting of a REA embargo on loans to Kentucky cooperatives.

The REA has also concluded debt restructuring agreements with the Illinois Valley Electric Cooperative in September 1989 (also involving a rate increase), the Western Illinois Power Cooperative in March 1989, and with the Wolverine Power Supply Cooperative in Michigan (possibly in 1987). The REA is in the process of finalizing a debt restructuring agreement with the Washington St. Tammany Electric Cooperative, Louisiana, which technically was and still is in a Chapter 11 situation. REA debt restructuring negotiations are also under way with the Cajun Electric Power Cooperative, Louisiana, and with the Deseret G&T, Utah. Neither of the latter two cooperatives is in Chapter 11 proceedings.

2. Status of Anti-CWIP Statutes

The majority of the states do not permit the inclusion of "Construction Work In Progress" within the "used and useful" capital investment on which utilities are permitted to earn a return. This does not necessarily arise from the existence of specific "anti-CWIP" statutes, but it is based on the interpretation of the commonly accepted "used and useful" standard for the valuation of "all property of every public utility actually used and useful for the convenience of the public..." Ind. Code § 8-1-2-6, emphasis added, see also Citizens Action Coalition of Ind., Inc. v. Northern Ind. Pub. Serv. Co., 472 N.E.2d 938 (Ind. App. 1984), aff'd, 485 N.E.2d 610 (Ind. 1985), cert. den'd, 476 U.S. 1137 (1986). A large number of states are reported as permitting "some" CWIP in utility rate bases, e.g., the District of Columbia, Indiana, and Pennsylvania permit the inclusion of CWIP in a utility's rate base for "pollution control equipment" (see Ind. Code §§ 8-1-2-6.1 et. seq., 8-1-8.7-1 et. seq.). A small number of states permit CWIP in utility rate bases under conditions that may threaten a utility's financial integrity (Texas and Idaho), and where a utility construction project has been "prudently planned and managed" (Texas). Ohio permits CWIP in the rate base when a construction project is 75% complete, and the Federal Energy Regulatory Commission (FERC) permits CWIP for all "pollution control equipment" and for 50% of "all other facilities" (see M. D. Luftig, G. B. Enholm, Electric Utility Regulation - Semiannual Review, Salomon Brothers Stock Research, February 21, 1989).

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The primary purpose of "anti-CWIP" statutes, and of the "anti-CWIP" interpretation of "used and useful" statutes, is the utility recovery from ratepayers of revenue requirements associated with utility investments in facilities that do provide service for the benefit of the ratepaying public. Utility investment in facilities "under construction" may be providing service in the future. Under this mechanism, utilities are obliged to make prudent and needed capital investments in construction projects that will render adequate and reliable services to the public in the future. The risks arising from unneeded utility construction, which could be abandoned, are thus minimized for ratepayers. Correspondingly, the risks of abandoned construction costs for utilities are minimized where the utilities obtain prior approval of their construction programs from regulatory authorities, and subject such programs to ongoing regulatory review.

3. Public Utility Commissions & Bankruptcy Courts

Public utility commissions are traditionally better equipped than bankruptcy courts to adequately balance the competing interests that are commonly found in the utility rate making process. This is predominantly due to the technical expertise that utility commissions possess in dealing with complex rate making issues, e.g., public utility commissions continuously employ technical experts whose sole function is to advise the commissions on rate making matters. Furthermore, utility commissions are intimately familiar with the operations of any particular utility in their respective jurisdictions, and with the unique characteristics of a utility's service territory. Since utility commissions are statutorily empowered to protect the public interest, they have a strong commitment in the continuous delivery of adequate and reliable supplies of utility services to the general economy. In this very important respect, the economic and social goals of state utility commissions inherently have a long-term horizon, and they are not confined by the narrow questions that often confront a bankruptcy court, i.e., public utility ratemaking does not involve only the "one-time satisfaction of creditors," but involves the protection of the much broader "public interest" on a continuous basis.

The protection of the broader public interest that is entrusted to state public utility commissions guarantees a better degree of impartial treatment of all the interested parties in the rate making process. Selected groups are not and cannot be used as the vehicles for the economic satisfaction of specific interests. In contrast, a bankruptcy court could always utilize the ratepayers as the vehicle for both the satisfaction of creditors and the financial stabilization of a bankrupt utility.

4. Concept of Federalism

The concept of federalism should be framed within the broad definition of "public utility rate making" rather than within the narrow scenario of "utility rate making under bankruptcy." If the concept of federalism were to be framed in such a way, clear boundaries of jurisdictional authority would easily emerge. Existing federal statutes, such as the Federal Power Act, can and do clearly define the scope of state and federal jurisdictional authority in utility rate making matters. Both state and federal utility regulators are concerned with similar matters (the protection of the broad "public interest" being their paramount concern), and they both possess similar technical abilities to resolve rate making issues. The involvement of federal bankruptcy

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courts in the rate making of bankrupt utilities will not only blur the federal and state jurisdictional delineation, but it may also infringe on the constitutional separation of powers, e.g., the bankruptcy court, a part of the federal judiciary, may be seeking to protect an executive federal agency that is a creditor to the detriment of legitimate state interests.

5. Different Treatment of Public Utility Corporations

Public utility corporations provide unique products to the general public which are absolutely essential for the operation of our general economy. These products, the various "utility services," cannot be easily substituted neither can they be easily supplied by entities other than the utilities themselves, e.g., industrial customers may be able to substitute electric power with alternative energy supplies, or they may even be able to generate their own electric power; such alternatives, however, do not exist for residential and commercial utility customers. Utility bankruptcies inherently threaten the continuous, adequate and reliable supply of utility services to the broad public and to the general economy. Interruptions of utility services do lead not only to economic damages for the recipients, but they also manifest concrete threats against the public's health and safety.

B. QUESTION OF SENATOR THURMOND

1. State Regulatory Agency Involvement in Reorganization Plans

State public utility commissions will by definition become involved in any reorganization efforts of a bankrupt utility. Existing statutory authority will oblige any state public utility commission to look at any utility's reorganization activities, irrespectively of whether S.46 becomes law, e.g., a state utility commission will be involved in examining and approving any refinancing plans (debt restructuring) that the utility may have, the state commission will oversee the disposition of utility assets so that the supply of utility services is not interrupted, and the state commission will continue to maintain its jurisdiction over the rates that the utility will charge to its ratepayers during and after the utility's reorganization. Of course, such state statutory authority will become a nullity if federal bankruptcy courts can lawfully preempt state public utility commissions in matters pertaining to the reorganization of bankrupt utilities, e.g., if the U.S. Supreme Court were to rule that federal bankruptcy courts indeed hold such federal preemption powers. It is this latter eventuality that S.46 is designed to prevent.

There can be several arguments against the preeminence of state public utility commission vis-à-vis the federal bankruptcy courts in cases of bankrupt utility reorganizations, e.g., the duration of proceedings before a state utility commission prior to the submission of a reorganization plan to the bankruptcy court; the possible appeal of a state utility commission decision to a state appellate court and the consequent effects of litigation delays on the reorganization of a bankrupt utility, etc. In this respect, S.46 may narrow the scope of state public utility involvement in bankrupt utility reorganizations by simply establishing the preeminence of state jurisdiction only over the rates of bankrupt utilities and the continuous provision of utility services, e.g., a federal bankruptcy court can still proceed with a reorganization plan leaving the state public utility commission to continue exercising its jurisdiction over the rates and the supply of utility services of any

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bankrupt utility (delineation of legitimate state economic, health and safety interests). Under such an arrangement, the jurisdictional boundaries of the bankruptcy courts and of the state public utility commissions will continue to be clear. In addition, state utility commissions will continue to focus on their traditional area of technical expertise in public utility ratemaking.

EKP/LEP/TNT/KDM/lep

August 16-18, 1989

Senator HEFLIN. Mr. Borson.

STATEMENT OF DAN BORSON

Mr. BORSON. Good morning. My name is Daniel Borson, and I am an energy policy analyst for Public Citizens Critical Mass Energy Project. I work on economic issues involving electric power generation and nuclear utilities. Public Citizen has a long history of working to maintain government and industry accountability, promoting States rights for local control of public services, and protecting consumers against drastic rate increases.

Public Citizen urges the subcommittee to support S. 46 because it embodies these three principles. This bill would protect ratepayers by ensuring that electric utilities do not misuse the bankruptcy filing procedure to evade State laws. Further, it would ensure that State public utility commissions retain their full regulatory authority in the event of bankruptcy.

State regulators are more accountable to ratepayers in their States than are Federal regulators and they are better acquainted with the specific conditions in their States. It is, therefore, in the public interest to keep control of local matters such as utility services in the hands of local and State officials wherever possible.

Should PSNH's proposed reorganization plan be accepted, the New Hampshire PUC would, in essence, be deprived of its regulatory jurisdiction in favor of the FERC. This stripping of local control over utility rates is not in the public interest. It has yet to be decided how much of the investment in the Seabrook nuclear plant will be deemed prudent and allow it to enter the rate base. The PUC has a history of more than 15 years of addressing this issue. A bankruptcy court should not be allowed to arbitrarily change the players midway in the game and decide to transfer that authority to the Federal Government.

Where now the PUC has jurisdiction over the final rates charged to the consumer, under the reorganization plan the FERC would regulate rates. The PUC would be virtually powerless to prevent a retail rate increase. We have strong reservations with the FERC regulating utilities in this manner. The FERC is not familiar with the local concerns involved. They lack direct accountability to ratepayers, and they are less likely to include the consumer's voice in the regulatory process.

It has long been accepted public policy that the protection of the public's well-being is best vested in State and local authorities. States have offices expressly for consumer advocacy and protection. There is presently no mechanism for any agency to intervene on behalf of consumers before the FERC or in the bankruptcy proceeding. It is also important that States and citizens of those States be able to decide their own energy policies and to enact laws to protect their ratepaying citizens with the assurance that those laws will be upheld and obeyed.

S. 46 should not be seen as a New Hampshire bill. While the most immediate effect of this bill would be on ratepayers in New Hampshire, it could benefit ratepayers in many other states. Several utilities around the country have recently experienced financial difficulties because of imprudent and uneconomic investments. If this bill is defeated, the result may be a climate where it is more attractive for utilities to file for bankruptcy to evade State regulations in order to secure higher rates.

S. 46 will help ensure that State and local control remains intact; that citizens remain involved in the regulatory process; and that consumers are protected from unreasonable rate increases. We urge your support for this important legislation. Thank you.

Senator HEFLIN. Thank you.

[The statement of Mr. Borson and answers to questions submitted by Senators Heflin and Thurmond follow:]



Testimony of
Daniel Borson
Energy Policy Analyst, Public Citizen

before the Subcommittee on Courts and Administrative Practices
United States Senate
Washington, D.C. 20510

July 26, 1989

Good morning. My name is Daniel Borson and I am an energy policy analyst for Public Citizen's Critical Mass Energy Project. I work on economic issues involving electric power generation and electric power utilities.

Public Citizen is a non-profit research and advocacy organization founded by Ralph Nader in 1971 to address a broad range of consumer and environmental issues. The Critical Mass Energy Project is Public Citizen's energy policy arm.

Public Citizen is dedicated to the principles of government and industry accountability, state's rights for local control of public services and protection against drastic rate increases. Therefore, Public Citizen urges the subcommittee to support the Electric Utility Bankruptcy Clarification Act (S. 46).

This bill would protect ratepaying consumers by ensuring that electric utilities do not misuse bankruptcy filing to evade state laws.

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Further, it would ensure that state public utility commissions retain their full regulatory authority in the event of bankruptcy. This is important because state regulators are more accountable to ratepayers in their states than are federal regulators. Moreover, they are better acquainted with the specific conditions in their state than are federal regulators, and it is therefore in the public interest to keep control of local matters such as utility services in the hands of local and state officials wherever possible.

Until recently, no utility has declared bankruptcy since the Great Depression. However, the issue has become important because one utility has declared bankruptcy, and a number of others have been or may be in the future on the verge. Public Service of New Hampshire, has filed for bankruptcy and is now attempting to use the bankruptcy process to circumvent state regulatory laws. Specifically, Public Service hopes its bankruptcy filing will enable it to evade a New Hampshire law which prohibits it from increasing its rates to recover its uneconomic investment in the Seabrook Nuclear Power Plant until the plant begins producing electricity.

The law in question concerns "Construction Work in Progress" investments or "CWIP." This "anti-CWIP" law prohibits such investments from entering the rate base.

As part of its bankruptcy filing, Public Service proposes to split itself up into three companies: a generation company, a transmission

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company and a retail company. This would, in essence, deprive the New Hampshire Public Utility Commission (PUC) of its regulatory jurisdiction, in favor of the Federal Energy Regulatory Commission (FERC).

Where now the PUC has complete jurisdiction over the final rates charged to the consumer, under the reorganization plan, FERC would regulate the wholesale rates of the transmission company. Public Service hopes FERC, which has no anti-CWIP policy, will allow a wholesale rate increase even before Seabrook operates. The PUC will then be virtually powerless to prevent a retail rate increase because retail rates are directly dependent on wholesale rates. Public Service could then increase its rates by a much larger amount than currently allowable under state law.

The passage of S. 46 would ensure that utilities could not misuse corporate restructuring to deprive ratepayers of those protections they currently enjoy and that ratepayers would be protected by state laws regardless of a utility's financial status.

S. 46 should not be seen as a "New Hampshire Bill." While the most immediate effect of this bill would be on ratepayers in New Hampshire, it could benefit ratepayers in many other states. Several utilities around the country have recently experienced financial difficulties because of imprudent and uneconomic investments: Middle South Utilities in Louisiana and Kansas Gas and Electric, for example.

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This bill would discourage them from also using a bankruptcy filing to evade state regulations in order to secure higher rates.

Even if S. 46 is enacted, a utility may still seek to challenge state laws in the courts. (Public Service tried this, and the courts upheld the state law.) We believe, however, that the complex process of a bankruptcy reorganization should not be used as a smokescreen for such a challenge.

Wherever possible states should retain their regulatory authority over public services. Should this authority be transferred to the federal government or to a bankruptcy court, the opportunities for ratepaying citizens to intervene on their own behalf is greatly diminished. States have offices expressly for consumer advocacy. No such entities exist either in the FERC or elsewhere in the federal government. It is also important that states and the citizens of those states be able to decide their own energy policies and to enact laws to protect their ratepaying citizens, with the assurance that those laws will be upheld and obeyed.

S. 46 will help ensure that consumers remain involved in the ratemaking process and protected from unreasonable rate increases.

We urge your support for this important legislation.

PUBLIC CITIZEN

Buyers Up ☐ Congress Watch ☐ Critical Mass ☐ Health Research Group ☐ Litigation Group
August 10, 1989

The Honorable Howell Heflin
Subcommittee on Courts and Administrative Practice
Senate Judiciary Committee
223 Hart Senate Office Building
Washington, DC 20510

Dear Senator Heflin:

Thank you for allowing me the opportunity to testify before your subcommittee on the "Electric Utility Bankruptcy Clarification Act," S. 46 on July 26.

The following are my responses to the additional questions asked by you and Senator Thurmond:

QUESTIONS SUBMITTED BY SENATOR HOWELL HEFLIN

1) "I appreciate your testimony which indicates that public utility bankruptcy is not just a problem found in New Hampshire. Are either of you aware of other states and other public utility companies who have encountered similar situations?"

In recent years, many public utilities have been close to bankruptcy:

** In 1983, the Washington Public Power Supply System (WPPSS), a consortium of 23 electric companies, defaulted on \$2.25 billion in bonds, but did not go bankrupt.

** Before its deal with the state of New York to close the Shoreham nuclear power plant, the Long Island Lighting Company (LILCO) said in a proxy statement that if it could not renegotiate its debts or obtain financing, the ensuing cash shortfall "would likely result in the company's bankruptcy." LILCO had spent \$4.1 billion on its Shoreham nuclear power plant and was seeking a rate increase.

** In 1984, Consumers Power of Michigan cancelled its \$6 billion Midland nuclear power plant. Consumers Power did not paid dividends to its investors for two years.

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** Public Service Co. of Indiana abandoned its \$7 billion Marble Hill nuclear power plant. The company ran out of money and the Public Service Commission refused to grant a rate increase for many months.

** Cincinnati Gas and Electric Co. cancelled its Zimmer nuclear power plant after an expenditure of \$1.6 billion because the plant would have cost another \$2.8 billion to \$3.5 billion to complete.

While there are currently no public utilities we are aware of facing immediate bankruptcy, many electric utilities are facing financial difficulties because of imprudent investments in large power plants:

** Kansas Gas and Electric was required to write off 50 percent of its share in the Wolf Creek nuclear power plant because the investment was deemed imprudent.

** Public Service of New Mexico's (PNM) security rating was downgraded as a result of its \$1.2 billion investment in its share of the Palo Verde nuclear power plant. The New Mexico Public Service Commission (PSC) was investigating the prudence of the investment. While PNM and the PSC eventually reached an agreement, the state attorney general may contest the settlement.

** By December 31, 1989, Gulf States Utilities will be almost \$190 million behind in dividend payments for preferred and preference stock because it had not been able to secure a rate increase for its investment in the River Bend nuclear power plant.

** In 1987, Niagara Mohawk (NiMo) took a \$755 million after-tax write off on its 41 percent share of the \$6.3 billion Nine Mile Point-2 nuclear reactor. At the same time, NiMo's Nine Mile Point-1 reactor was in a 17-month outage, limiting the company's income. As a result, the company's first quarter earnings in 1989 dropped almost 40 percent from 1988 levels. Additionally, the other utility co-owners of the reactor are currently seeking to seize control of the management of the plant because they are dissatisfied with NiMo's performance.

2) "Are Anti-Construction-Work-In-Progress statutes commonly found in the United States? What is the primary purpose of these statutes? What is the common view of public utility commissioners as to these types of statutes?"

I believe Mr. Monk is better qualified to answer these questions. I can say however, that anti-CWIP laws are designed to protect ratepayers from the financial risks involved in an investment in large-scale power projects by requiring investors to shoulder the risk until the projects produce electricity. They also lessen the likelihood of

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excess costs being passed on to consumers without regulatory review, and they serve as a break on utilities building unneeded or excessively costly generating capacity.

- 3) "Do you believe that public utility commissions are better equipped than bankruptcy courts to balance and weigh competing interests found in the ratemaking process? Why?"

Bankruptcy courts are established primarily to balance the interests of the bankrupt company and its creditors. Customers of the company are usually excluded from the process. In the case of a regular company (not a public utility) there is usually a competing company where customers can go if the company's prices rise too high. In the case of a regulated monopoly, such as a public utility, it is imperative that the ratepaying customers' interests be considered when setting rates for a bankrupt utility.

A state public utility commission is more familiar with the specific conditions in its state than is a federal bankruptcy court, and it has more experience in balancing the competing interested parties. The public utility commission should therefore retain its regulatory authority, even during a bankruptcy. A bankruptcy court also lacks expertise in rate-making decisions and issues.

- 4) "What role do you believe the concept of federalism should have in determining public utility rates?"

Wherever possible, the price consumers pay for utility services should be set on the state and local level. While there may at times be some overriding national policy which would take precedent (such as a war or a national energy crisis), state and local public policy entities are better able to consider all the conditions and interests within the area under their jurisdiction. Federal regulators, on the other hand, must also weigh the interests of parties in 49 other states. The federal government should not be micro-managing state or local situations when there is already a regulatory body which serves that purpose.

- 5) "The effect of this legislation is to treat public utility corporations differently from other corporations. Why should these companies be treated differently and subject to a different standard?"

Public utility corporations are inherently different entities from most other corporations: public utilities are regulated monopolies, and their customers are bound by geography into buying their services. As a result, this monopolistic condition is balanced by state and local

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regulatory agencies that protect the ratepaying consumers from high prices, while ensuring that the utility companies receive a fair return on their investments. Therefore, a different standard must apply to regulated monopolies than applies to other companies whose customers can almost always patronize the competition.

QUESTIONS SUBMITTED BY SENATOR STROM THURMOND

1) "The Public Service Company of New Hampshire's plan of reorganization places a portion of its rates under the jurisdiction of the Federal Energy Regulatory Commission. Do you believe that the Federal Energy Regulatory Commission will be any less inclined than State regulatory authorities to protect the public interest when approving utility rates?"

The FERC may be less inclined to consider the ratepaying public's interest than State regulatory authorities for the following reasons:

** State regulators are better acquainted with the specific conditions in their states than are federal regulators. It is very difficult, if not impossible, for the FERC to be aware of the unique local issues in all 50 states.

** State regulators are more accountable to ratepayers in their state than are federal regulators because they are either appointed by the governor and approved by the state legislator or elected directly by the voters. Federal regulators, who are appointed by the President, must also consider the interests of 49 other states.

** States have an official who can intervene before state public utility commissions on behalf of ratepayers (usually a consumer protection official or the state attorney general). There is no equivalent official representing state ratepayers' interests before the FERC.

2) "If the policies of Federal Energy Regulatory Commission are objectionable and the two-tiered regulatory structure insufficient to protect consumers against "rate shock," would it not be better to re-examine the broader issues related to energy regulation as opposed to amending the Bankruptcy Code in response to the case currently pending?"

It may indeed be wise to re-examine the entire issue of energy regulation, and at some point this should be undertaken. Now, however, a utility is trying to use the a gap in the Bankruptcy Code to place itself under regulatory jurisdiction that will be more favorable to it. While energy regulation with respect to the Bankruptcy Code is not as broad an issue, it is nevertheless an important one which needs to be

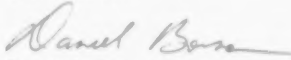
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addressed now. Once this is done, Congress can then proceed to the business of re-examining the energy regulatory structure. The two issues are not mutually exclusive.

I trust these comments satisfactorily answer your questions. Thank you again for the opportunity to participate in these important proceedings.

Sincerely,



Daniel Borson
Nuclear Economics Analyst
Public Citizen's Critical Mass
Energy Project

Senator HEFLIN. Mr. Whelan, we would be delighted to hear from you now, Judge Whelan.

STATEMENT OF ROGER WHELAN

Mr. WHELAN. Thank you, Mr. Chairman, for the opportunity to appear here with you this morning. I am testifying on behalf of the American Bankruptcy Institute, a bipartisan nonprofit educational institute. However, the statements that I make here today are my own. In my opinion, S. 46 as presently drafted would cause a considerable amount of delay, confusion, and expense in connection with any public utility reorganization. I certainly agree that the State regulatory authority has to be included in the reorganization process in a meaningful role in its capacity as protector of the ratepayer's interest.

However, I would point out and as previously pointed out in Mr. Levin's testimony, the structure of the Bankruptcy Code, in my opinion, clearly provides for protection of such State interest. As we know, a chapter 11 reorganization takes a considerable amount of time, expense, and effort on the part of all parties. Some of these greatest costs are the administrative expenses including professional fees. To require a complete review of the debtor's utility's reorganization plan by a State regulatory agency prior to its submission to the bankruptcy court would, in my opinion, involve clearly substantial and additional cost to an already expensive reorganization proceeding.

This system would further result in significant delays which, if such occurred, might translate into loss for consumers due to possible reductions in level of service. A bankruptcy court and a regulatory body each have their own special talents that should be drawn upon in connection with the reorganization process.

The regulatory agency's forte is traditionally and primarily in connection with rate setting and assuring that the interests of electric ratepayers are protected. State regulators, however, do not have expertise in the administration and review of a complicated reorganization plan which traditionally has been the recognized expertise of the U.S. bankruptcy court.

The bankruptcy courts are proficient in the processes of asset sales, financing, lien determinations, and other issues which arise in connection with the reorganization process. I think that the present legislation as proposed would clearly split these functions down the middle and we would have two ball playing fields, so to speak, much to the detriment of any reorganization process.

Bankruptcy courts themselves, I think, have consistently considered the public interest in reaching decisions. The bankruptcy court itself is a court of equity, and whenever it makes decisions, it makes those determinations based on the balancing of the interest of creditors, the debtors, consumers, and in your larger cases such as this, the public at large. In fact, the very essence of equity is the balancing of all interests in a case. And clearly the Bankruptcy Code itself provides for that type of participation.

In railroad reorganizations, the Bankruptcy Code specifically mandated that the bankruptcy court is to protect the public interest. Now although railroads are a type of public utility and they themselves are specifically dealt with under subchapter 4 of chapter 11, the omission of such a clause for electric utilities does not in any way derogate from the bankruptcy court's attention to the public interest at large.

In fact, as pointed out in prior testimony of Mr. Levin, the history of the Bankruptcy Reform Act, I think, is clear that what was to be avoided in connection with railroad reorganizations was to avoid a two-tier process of having the regulator in the first instance essentially become involved in certifying a plan of reorganization. Congress had the foresight to provide for in the Bankruptcy Reform Act of 1978, to provide for exclusive bankruptcy court approval of the reorganization plan. And therefore, transferred from the ICC to the court authority to authorize, in addition, mergers, the modification of the debtor's financial structure, the issuance and sales of security.

Interestingly enough, these are also areas that are usually within the purview of a State public utility commission, and the proposed legislation would also require prior approval by the State agency in those matters. That in itself would clearly be, in my opinion, counterproductive to an already comprehensive statute which deals and provides for the protection of the rights of all parties.

I would hope that these remarks will be of some assistance to this committee in maintaining an efficient and equitable judicial and administrative system, and I thank you, gentlemen, for the opportunity to appear here today.

Senator HEFLIN. Thank you.

[The statement of Mr. Whelan and answers to questions submitted by Senator Heflin follow:]

STATEMENT
OF
THE HONORABLE ROGER M. WHELAN

BEFORE THE UNITED STATES SENATE
SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE
OF THE COMMITTEE ON THE JUDICIARY

HEARINGS ON THE ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT

July 26, 1989

Mr. Chairman and members of the Committee:

I am Roger M. Whelan, a practicing bankruptcy and insolvency attorney with the law firm of Verner, Liipfert, Bernhard, McPherson and Hand in the District of Columbia. Prior to my present private practice, I served as a United States Bankruptcy Judge. I was first appointed as a Referee in Bankruptcy for the District of Columbia on July 1, 1972. I was on the bench when new bankruptcy rules were enacted in 1973 and continued to serve as a Bankruptcy Judge under the new bankruptcy code when the latter first became effective in 1979. I also served on the United States Bankruptcy Court for the District of Maryland from August, 1981 through December, 1982. I served on the bench until my resignation on December 1, 1983. I was the presiding judge in the Auto-Train Corporation case, the first railroad reorganization case under the new bankruptcy code, and the PATCO Chapter 11 case. I have written and lectured extensively on various bankruptcy matters. I am a Distinguished Lecturer at the Columbus School of Law (Catholic University) where I have taught continuously since 1975.

Although I am here today on behalf of the American Bankruptcy Institute, my views are my own. The American Bankruptcy Institute is an association of academicians, judges, practitioners and public policy makers who have a professional interest in the field of bankruptcy law and practice, and particularly in the organization and efficiency of the nation's bankruptcy courts. The American Bankruptcy Institute is a

bipartisan, non-profit educational institute.

The Electric Utility Bankruptcy Clarification Act, S-46, as presently drafted, in my opinion, will cause a considerable amount of delay, confusion, and expense in a public utility reorganization. I agree that a State regulatory authority ought to be included in the reorganization process in a meaningful role in its capacity as protector of the ratepayer's interests. I would like to suggest an alternative measure that would impose less onerous burdens on the debtor than the proposed legislation does.

A Chapter 11 reorganization takes considerable time, expense and effort. Some of the greatest costs of bankruptcy cases are the administrative expenses, including professional fees. To require a complete review of a debtor utility's reorganization plan by a state regulatory agency prior to its submission to a bankruptcy court would involve substantial costs. This system could result in significant delays, which, if such occurred might translate into an loss for the consumers due to possible reductions in the level of service or delays in reorganization that would otherwise disrupt service or increase rates.

A bankruptcy court and a regulatory body each have specialties and talents that should be drawn upon. The regulatory agency's forte is primarily in rate setting and in assuring that the interests of electric ratepayers are protected. State regulators do not have expertise in the administration and review of a complicated reorganization plan, which traditionally

has been the recognized expertise of the bankruptcy court. The bankruptcy courts are proficient in the processes of asset sales, financing, lien determinations and other issues commonly arising in corporate reorganizations. Each group should perform the functions that it can do best.

Bankruptcy courts consistently consider the public interest in reaching decisions. A bankruptcy court is a court of equity. Whenever it makes decisions it should make determinations based on the balancing of the interests of the creditors, the debtors, consumers and, in larger cases, the public at large. In railroad reorganizations the Bankruptcy Code specifically mandates that the bankruptcy court is to protect the public interest with equal determination as it does with the private rights of debtors, creditors and equity security holders. Although railroads, a type of public utility, are specifically dealt with in a new subchapter of the Code, the omission of such a clause for electric utilities does not derogate from the bankruptcy court's attention to the public interest in such cases.

The Bankruptcy Reform Act of 1978 is in many ways similar to the present proposal that we have with the electric utilities. The I.C.C. was active in railroad reorganizations under the old section 77 of the Act. In that section, the I.C.C. was the initial reviewing body of reorganization plans presented by the parties. Only upon certification by the I.C.C., would the parties then be able to present the plans to the district court for confirmation. This process was highly criticized and led

Congress to restructure railroad reorganizations under Section 1161 et seq., by eliminating the I.C.C.'s role in certification of the reorganization plan. Congress had the foresight to provide in the bankruptcy code for exclusive bankruptcy court approval of the reorganization plan. Congress has additionally transferred from the I.C.C. to the bankruptcy court authority to authorize a merger, the modification of the debtor's financial structure, and the issuance and sales of securities under a plan. Some of the problems identified with respect to railroad reorganizations may occur with regard to the present bill.

Reorganization should remain in the bankruptcy court. If a reorganization plan modifies, restricts or divests the regulatory authority, the regulator has a right to be heard or the right to file objections as a party in interest to the plan of reorganization. A workable alternative would be to amend section 1129(A)(6) to provide the State regulatory authority with final approval of any plan of reorganization.

In conclusion, I do not oppose, and clearly the existing bankruptcy code does not oppose, the ongoing and supervisory role of a regulator in the affairs of an electric utility. However, I would urge the Congress not to create what was dismantled with railroad reorganizations in devising a two step review process. Reorganizations must be kept as efficient and expedient as possible.

I hope that these remarks will be of some assistance in your efforts to maintain a efficient and equitable judicial and administrative system.

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August 26, 1989

Honorable Howell Heflin
United States Senate
Subcommittee on Courts & Administrative Practice
Senate Judiciary Committee
223 Hart Senate Office Building
Washington, D.C. 20510-6275

Dear Senator Heflin:

In response to the questions propounded to me in your letter of August 3, 1989, concerning S. 46, the "Electric Utility Bankruptcy Clarification Act," I am setting forth on a separate sheet my responses. I trust that the responses provided will be of assistance to you and the subcommittee in analyzing the provisions and effects of S. 46.

With my best wishes, and thanks to you for providing me with an opportunity to provide these responses, I remain

Sincerely,

Roger M. Whelan
Roger M. Whelan

Attachment - Responses

RESPONSES FROM JUDGE WHELAN
TO SENATOR HOWELL HEFLIN
CONCERNING S. 46

QUESTION 1. WOULD YOU COMMENT ON THE RETROACTIVITY PROVISION
OF S. 46?

RESPONSE 1. Whenever parties embark upon a particular course of legal action -- e.g., the initiation of a major Chapter 11 case by Public Service of New Hampshire ("PSNH") -- those parties have a right to rely reasonably upon the status of law at the time they undertake their legal action. Aside from serious questions raised by the possible construction of retroactive legislation as unconstitutional bills of attainder, it is unwise, in my opinion, to legislate on a purely reactive basis with respect to a particular dilemma confronting a particular entity or a narrow segment of the private sector.

Whatever circumstance gave rise to the particular problem confronting the entity, it should receive serious, deliberate and reasoned consideration. Only in the most extraordinary situation should legislation be enacted to address a problem of a particular individual, entity or limited element of our society. PSNH, in my view, does not present such an extraordinary situation. Indeed, its apparent ability to progress towards reorganization under the existing form of Chapter 11 is testimony to Congress' success in devising a reorganization statute flexible enough to meet the widest possible array of demands. Except for discrete groups whose proverbial oxen are being gored,

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those who participate in Chapter 11 cases generally find no legal or practical justification for selective modification of Chapter 11.

QUESTION 2. IF S. 46 WERE ENACTED, WOULD SUCH AUTHORITY IN THE HANDS OF THE REGULATORY AGENCY SERVE TO HINDER THE ABILITY OF A COMPANY TO REORGANIZE?

RESPONSE 2. In my opinion, the proposed legislation would impact adversely on the ability of the debtor to reorganize under Chapter 11. Putting to one side the debate over the retention of complete control of basic utility issues by a public utility commission, the debtor's primary reorganization efforts are logically directed towards a single judicial forum -- the United States Bankruptcy Court. To bifurcate the debtor's focus of its time, energies and resources in the reorganization process to both an administrative and a judicial forum, where many matters may be of an overlapping nature, is unproductive and expensive for any reorganizing entity. Because Chapter 11 cases are already expensive and time-consuming, for debtors and creditors alike, the creation of a new, additional administrative process would merely exacerbate and compound these problems. As I have noted in response to other inquiries below, there may be other, more economical alternatives.

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QUESTION 3. JUDGE WHELAN, IN YOUR OPINION AS A FORMER BANKRUPTCY JUDGE, WOULD S. 46 INTRUDE UPON THE ABILITY OF A COURT TO ACHIEVE A SUCCESSFUL PLAN OF REORGANIZATION?

RESPONSE 3. The reasons given above and during my testimony (dealing with the Bankruptcy Code's approach to reposing basic responsibility for approval of the reorganization process -- except for rate approval -- in the United States Bankruptcy Court) provide ample authority for rejecting S. 46. As pointed out in my testimony, for example, the old railroad reorganization provisions of the former Bankruptcy Act of 1898 required the approval of a reorganization plan by the Interstate Commerce Commission as well as the Bankruptcy Referee. As a result of the Bankruptcy Reform Act of 1978 (the Code), the reorganization process was committed to a single forum -- the United States Bankruptcy Court. In my opinion, this change from the old Act has been a salutary one, as evidenced by the successful reorganization efforts of railroads under the Bankruptcy Code. It also demonstrates Congressional sagacity in consolidating reorganizations before a single forum.

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QUESTION 4. IS THERE A MIDDLE GROUND HERE, BETWEEN GRANTING THE STATE REGULATORY AGENCY COMPLETE APPROVAL OF THE PLAN AND ALLOWING THE UTILITY TO CIRCUMVENT STATE REGULATORY PROCEDURE?

RESPONSE 4. Please bear in mind that I am not, in any way, holding myself out as an expert in the area of utility law (although I have had frequent occasion to testify before various public utility commissions). However, I feel that if considerably more experience and research than exists now should indicate that state regulators need to have final approval of a plan of reorganization, then clearly that need should be accommodated. However, the pending bill is not justified by anything other than bare reflex. As I have stated, leaving the state regulator as the final authority on all aspects of the reorganization process -- as S.46 contemplates -- would needlessly bifurcate Chapter 11 proceedings, and hinder and delay the achievement of the ultimate goal of an expeditious and economical reorganization. It makes more sense to have the reorganization process take place in a single forum -- i.e., the Bankruptcy Court -- as envisioned by Congress in consolidating the reorganization provisions of the old Bankruptcy Act when enacting the existing Code provisions.

One alternative to S. 46 would be to provide the Public Utility Commission with some form of participatory veto power over any proposed Chapter 11 plan, exercisable before the Bankruptcy Court. The parties to the reorganization would negotiate with this veto power in mind; and the chances for

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achieving a consensual plan would be enhanced if the concerns of the regulator were made known during the negotiation processes. It is counter-productive to permit intrusion and oversight at every level of the reorganization process by the public utility commissions, and they already have standing to participate as parties in interest. However, such regulatory participation should not supplant the experience, expertise and administrative capabilities of the Bankruptcy Courts. The administrative process is in an entirely different type of forum than the judicial process and the ultimate goal of achieving successful reorganization will be far better achieved by placing reorganization issues where they properly belong -- within the forum of the United States Bankruptcy Court.

QUESTION 5. DO YOU BELIEVE THAT A SEPARATE CHAPTER FOR PUBLIC UTILITY BANKRUPTCIES IS NECESSARY?

RESPONSE 5. At this time, in the absence of substantial further study, I do not believe that a separate Chapter of the Bankruptcy Code for public utility bankruptcies is justifiable. It behooves Congress not to rewrite the Bankruptcy Code every time some particular vocal constituency urges upon Congress some alleged manifest injustice or infirmity built into the Bankruptcy Code. While it is conceivable that there will be situations where the Bankruptcy Code is insufficient or runs afoul of

subsequent legislation, Chapter 11 is flexible enough, and the Bankruptcy Courts facile enough, to handle most imaginable circumstances without special-interest tinkering.

PANEL V

QUESTION 1. HOW IS THE PUBLIC INTEREST PROTECTED IN A CHAPTER 11 REORGANIZATION PROCEEDING? FROM THE TESTIMONY WE HAVE HEARD TODAY, IT APPEARS THAT THE STATE REGULATORY AUTHORITY MAY BE THE SOLE REPRESENTATIVE OF INDIVIDUAL RATE PAYERS.

RESPONSE 1. The Bankruptcy Code (11 U.S.C. §1109) and Bankruptcy Rule 2018 clearly provide for standing and participation by a state regulator in a Chapter 11 case. In any Chapter 11 case, the United States Bankruptcy Court must consider all interests of appearing parties. Although there is no specific statutory mandate for consideration of the public interest -- as appears in the railroad reorganization subchapter of Chapter 11 -- the Bankruptcy Court, in my opinion, cannot ignore rate payer interests in the reorganization process.

For example, in Section 1129 of the Bankruptcy Code (which governs approval of Chapter 11 plans of reorganization), the Code states that a plan under Chapter 11 can only be approved by the Bankruptcy Court if it is "not by any means forbidden by law." Also, Section 959 of Title 28, U.S. Code, specifically requires

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that a trustee or debtor in possession under Chapter 11 "shall manage and operate the property in his possession . . . according to the requirements of the valid laws of the State in which such property is situated" Both of these statutory provisions, among others, encompass contemplation of the public interest as manifest in applicable non-bankruptcy laws. I believe that these provisions accord more than ample opportunity for the public interest to be considered and respected.

QUESTION 3. THE REFORMS SOUGHT BY S. 46 WOULD APPEAR TO AFFECT THE OUTCOME OF ONE PARTICULAR CASE. ARE THERE ANY OTHER SIMILAR CASES BEFORE THE COURTS WHICH COULD BE AFFECTED BY ENACTMENT OF S. 46?

RESPONSE 3. To my knowledge, PSNH is the only investor-owned utility presently in Chapter 11. In view of the fact that there are apparently no other investor-owned utilities presently threatening to file imminently for relief under Chapter 11, it appears that S. 46 is directed to affect the outcome of only one particular case. (To some extent, this may implicate "separation of powers" questions, inasmuch as such action by Congress can be seen as legislative intrusion into pending judicial matters. This is an extraordinary complex question, though, and a thorough review of it would vastly exceed the scope of this set of replies.) The only other Chapter 11 cases which S. 46 might impact (with respect to the preservation of the role of the state

regulator) are several small electric co-op utilities that have sought relief under Chapter 11. However, no pending case, or foreseeable case, would be as dramatically affected by S. 46 (if retroactivity is appropriate) than PSNH. As I have noted above, I see no reason to make precipitous changes to the Bankruptcy Code merely as a reflexive reaction to the PSNH case alone. More study, deliberation and analysis is required before substantive and procedural changes to Chapter 11 in this context are justified.

Senator HEFLIN. Mr. Rosen.

STATEMENT OF LEONARD M. ROSEN

Mr. ROSEN. My name is Leonard Rosen. I am with the New York law firm of Wachtell, Lipton, Rosen & Katz. I am not involved in the Public Service of New Hampshire case. I appear on behalf of the National Bankruptcy Conference of which I am the chairman. I would address only a single question, which is the question that the chairman posed at the beginning, and I think S. 46 poses the question: who is to have ultimate control of a chapter 11? Is it to be the bankruptcy court or is it to be a State agency representing a particular constituency?

I do not think chapter 11 will work unless the court is the ultimate repository of control over the case. And I think what S. 46 does is create two bodies that will attempt to deal with this, but it gives this veto power to a State agency, and I do not think chapter 11 as designed can work. If, in fact, public utilities or electric utilities need some special, unique treatment, then they do not belong in chapter 11.

There are entities that are now exempt from chapter 11: banks, S&L's, and a lot of other entities. It seems to me that if these entities are to stay within chapter 11, then it is wrong to give a single public agency which represents a single constituency a veto power over the case. A case involves many constituencies of which the ratepayers are only one, and it seems to me the court is the proper place in which those interests should be balanced. And giving a veto power to a state agency just makes it unworkable. Thank you.

[The statement of Mr. Rosen and responses to followup questions submitted by Senators Heflin and Thurmond follow:]

STATEMENT OF
LEONARD M. ROSEN
ON S. 46
HEARINGS BEFORE THE SENATE SUBCOMMITTEE ON COURTS
AND ADMINISTRATIVE PRACTICE

JULY 26, 1989

My name is Leonard Rosen. I am a partner in the New York City law firm, Wachtell, Lipton, Rosen & Katz and I am an adjunct professor at New York University School of Law. My specialty in practice, teaching, writing and lecturing is in the areas of out of court workouts and reorganization of financially troubled businesses under chapter 11 of the Bankruptcy Code. I appear before this Subcommittee on behalf of the National Bankruptcy Conference of which I am Chairman.

The National Bankruptcy Conference is an organization of judges, lawyers and law professors whose professional interest is in bankruptcy and reorganization law. The active membership, totaling about 65, is geographically diverse and is representative of the various constituencies normally involved in cases under the Bankruptcy Code, such as, debtors, unsecured creditors and secured creditors. The principal purpose of the Conference is to seek the improvement of bankruptcy law and practice through the review of existing and proposed legislation and rules. The Conference has assisted the Congress on innumerable occasions through testimony at hearings, reviewing draft legislation and proposing legislation.

The National Bankruptcy Conference considered S. 46 at its mid-year meeting in March, 1989 and, after discussion, adopted a resolution recommending against the enactment of the bill into law. The Conference has consistently opposed legislation which would benefit particular special interests

at the expense of a viable reorganization process and of other parties in interest in a reorganization case. The Conference believes that the Bankruptcy Code passed by the Congress in 1978 was well conceived and represents a very careful balancing of interests of the various groups involved in reorganization cases. Many days and months of hearings were had before Congressional committees concerning the substantive provisions of the Code and many days and months, even years were devoted to the drafting of the statute by Members and their staffs. Much of the conceptual underpinning for the Code was derived from the extensive work of a Congressional and Presidential Commission appointed in 1970 to study the bankruptcy laws of the United States and which filed a report and draft bill in 1973.

Piecemeal amendments to the Code (or to statutes which directly affect Code cases) designed to respond to an immediate problem of a particular party, public or private, in a particular bankruptcy case are simply not an appropriate way to deal with a statute that will have application in many more cases and whose provisions often have a significant impact on proposed transactions of entities not in any bankruptcy case and on the way in which parties having an interest in troubled debtors may seek to work out their problems without resort to the bankruptcy court. Such amendments, while responding to the needs of one of the constituencies involved in a case, adversely affect other constituencies involved in the case. Because they are designed to further the special interests of a particular group their impact on the overall reorganization process is downplayed or ignored. The deliberate thought, careful consideration and balancing of interests which should be the

essential ingredient for significant amendments to the reorganization process simply does not occur.

S. 46 appears to be an example of such legislation. The design and intent of S. 46 appears to be to block the currently proposed reorganization plan of Public Service Company of New Hampshire and to enable the State of New Hampshire to have a veto any other plan, all for the benefit of the electricity consumers of that particular state.

Congress in passing the 1978 Bankruptcy Code very specifically sought to diminish the impact of governmental agencies on the reorganization process. In particular, the role of state regulatory agencies over public utilities in a reorganization proceeding was reduced from the level that existed under Chapter X and the role of the ICC over railroads in a railroad reorganization case was reduced from the level that existed under Section 77 of the former Bankruptcy Act. We believe that the reduction of control was intended to avoid the inordinately lengthy proceedings which often plagued efforts by railroads and public utilities to reorganize under the Bankruptcy Act and to avoid agencies having near absolute power over matters having an impact far beyond their usual areas of regulatory concern and expertise. In the design of Chapter 11 of the 1978 Code an extraordinary amount of effort was devoted to streamlining the reorganization process so as to avoid giving any one constituency the ability, through an obstructive litigation strategy, a veto power or any other means to cause such delay and expense in the resolution of the case as to make reorganization not feasible without making whatever concession was sought by the objecting constituency. Giving

state regulatory agencies an absolute veto over any plan of reorganization of an electric utility is certainly inconsistent with the basic concept underlying chapter 11 of the Code, namely that parties in interest be given a fair, level playing field on which to negotiate a plan of reorganization. Such a right of approval exercised in such manner as to fully protect the interests of the constituency represented by state regulatory agencies might well make it impossible to meet the confirmation standards of §1129(a) and (b) of chapter 11 which mandate certain minimum distributions to creditors and would provide no means to balance the interests of consumers, creditors, employees and equity holders. If Congress in fact determines that such agency control over electric utilities is in the public interest then a better solution may be to attempt to devise a workable comprehensive reorganization statute specifically designed for electric utilities which contains such control provisions. Modifying chapter 11 as it now exists to give a veto power over plans to a state regulatory agency makes chapter 11 unworkable for electric utilities and is not a satisfactory solution. Those financial institutions who arrange for and participate in the financing of electric utilities, and suppliers to and other creditors of electric utilities should certainly be heard from as to any possible impact of the proposed legislation on their existing and potential future relationships with electric utilities.

Furthermore, it is not clear that S. 46 is necessary. Section 1129(a)(6) of chapter 11 of the Bankruptcy Code as it now exists provides for the approval by any governmental regulatory commission with jurisdiction of the rates to be provided for in any plan of reorganization. In addition, 28

U.S.C. §959(b) provides ". . . [a] trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof." These provisions appear to provide a reasonable balance between the interests of state regulation and the interests of reorganizing the debtor.

S. 46 makes its provisions retroactive and applicable to cases pending on the date of its enactment. Generally, Congress has been very careful not to make legislation retroactive because to do so is viewed as inequitable, violative of a sense of fair plan and to sometimes raise constitutional issues. In this case it also shifts a process that is and should be one of direct bargaining between the interested parties within a judicial framework into a political arena. The Bill, if passed, should be made applicable only to cases filed on and after its effective date.

NATIONAL BANKRUPTCY CONFERENCE

*(A voluntary organization composed of persons interested in the
improvement of the Bankruptcy Code and its administration.)*

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September 13, 1989

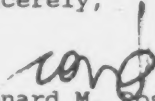
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Senate Judiciary Committee
223 Hart Senate Office Building
Washington, D.C. 20510

Gentlemen:

Enclosed please find my responses to questions submitted by Senators Strom Thurmond and Howell Heflin regarding my testimony before the Subcommittee on Courts and Administrative Practice on legislation concerning S. 46, the "Electric Utility Bankruptcy Clarification Act."

If you have any further questions or need further additional information, please do not hesitate to call me.

Sincerely,


Leonard M. Rosen
Chairman

LMR/meb

Questions Submitted by Senator Howell Heflin

1. As mentioned in my prepared statement, filed in the record of this hearing, making an amendment to the Bankruptcy Code retroactive and applicable to pending cases is at least inequitable and at most can be unconstitutional. It is something that should not be done without a good deal of research with respect to its constitutional implications and careful thought as to its basic fairness. In addition, retroactivity puts the political process into the middle of an ongoing judicial proceeding. It can be viewed as one party to a litigation attempting to have Congress give it a victory it cannot achieve in the courts. This is clearly not desirable. Retroactivity also defeats the expectations of the parties who rely on existing law to govern their actions. S. 46 should not be made retroactive.

2. If S. 46 were enacted it would make it virtually impossible for an electric utility to reorganize without the approval of the state regulatory agency. This would hinder the ability of a company to reorganize because it would deprive the bankruptcy court and district court of the jurisdiction needed to appropriately regulate the reorganization plan process.

The required reorganization plan approval of the state regulatory agency would be the subject of consideration by that agency in accordance with applicable state law and procedures essentially intended to protect the constituencies to which the agency would be answerable, presumably, ratepayers and possibly the executive and legislative branches of the state government. The positions of one or more of suppliers, bondholders, stockholders, lessors, taxing authorities, employees and others having an interest in the reorganization case could receive little or no consideration; the standard used to determine the agency approval or disapproval would necessarily be different from the standards for confirmation of a reorganization plan provided for in the Bankruptcy Code.

There could well be litigation before the state regulatory agency and appeals relating to the state approval process all in addition to the bankruptcy court plan confirmation process. The requirements of the state agency might make any plan incapable of being confirmed in accordance with applicable bankruptcy law. Neither the bankruptcy court nor the Supreme Court of the United States (which is the ultimate judicial body interpreting bankruptcy law), would be able to override the decisions of the regulatory agency.

3. There is the possibility for a middle ground position that recognizes substantial authority in state regulatory agencies. The current provision in the Bankruptcy Code in fact represents a middle ground. The Code requires regulatory agency approval of any rate change that may be

proposed by a plan of reorganization pursuant to section 1129(a)(6). This provision alone gives to the agency sufficient leverage during the course of a chapter 11 case to influence in a major way any proposed restructuring. Another middle ground possibility would be to clearly give the state regulatory agency standing to appear and be heard in the reorganization case on behalf of ratepayers and to require the bankruptcy court to find, as a part of the confirmation process, that the plan adequately considers the interests of ratepayers in addition to the other required findings.

4. Considering the lack of experience with and the lack of any significant number of public utility bankruptcies, I would not favor attempting to construct a separate chapter for public utility bankruptcies at this time. I believe any statutory changes attempted should seek a middle ground within the current chapter 11 structure. Care must be taken, however, to avoid giving state regulators a veto over the reorganization process.

Questions Submitted by Senator Strom Thurmond

1. The public interest consisting of ratepayers should be represented in a reorganization case by the state regulatory agency and such agency should be given standing to accomplish such representation. This could be accomplished through an expansion of Rule 2018(b) of the Federal Rules of Bankruptcy Procedure (FRBP) which now provides that the Attorney General of the State "may appear and be heard on behalf of consumer creditors if the court determines the appearance is in the public interest. . . ." Even without an amendment to the FRBP, Rule 2018(a) provides that the court, for cause, may permit "any interested party to intervene generally or with respect to any specified matter" and, in fact, the bankruptcy court in New Hampshire has permitted the state regulatory agency in the P.S.N.H. to so intervene. In addition to such representation in the case generally that agency's responsibilities and the public interest are now protected by section 1129(a)(6) of the Bankruptcy Code which does not permit a plan of reorganization to be confirmed unless the agency has approved any rate change provided for in the plan.

2. See response to Question 1 of Senator Heflin.

4. The existing provisions of chapter 11 deal adequately with a utility reorganization. The provisions of section 1129(a)(6) require the state regulatory agency to approve any rate change provided for in the plan. This gives the regulatory agency the ability to protect ratepayers.

Senator HEFLIN. Thank you. I am going to submit my questions in writing to each of you, and we appreciate your prompt response.

Senator GRASSLEY. I do not have any questions of this panel.

Senator HEFLIN. All right. Fine. Thank you. We would also like to include for the record without objection a statement from the Edison Electric Institute and letters from Public Citizen and the Environmental Action Foundation.

[Submissions for the record follow:]

STATEMENT OF
THE EDISON ELECTRIC INSTITUTE

ON

S.46,
THE ELECTRIC UTILITY BANKRUPTCY CLARIFICATION ACT

BEFORE THE
SUBCOMMITTEE ON COURTS AND ADMINISTRATIVE PRACTICE
COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

July 26, 1989

Mr. Chairman and members of the Subcommittee, the Edison Electric Institute (EEI) appreciates the opportunity to present its views on S.46, the "Electric Utility Bankruptcy Clarification Act."

EEI is the association of electric companies. Its members serve 95 percent of all customers served by the investor-owned segment of the industry. EEI members generate approximately 77 percent of all electricity in the country and provide electric service to 73 percent of the nation's ultimate electricity customers.

We believe S.46 is a fundamentally flawed bill, and EEI strongly urges this Subcommittee to reject it. Undoubtedly provoked by the bankruptcy of the Public Service Company of New Hampshire, this bill is undeniably part of the increasing -- and very troubling -- trend of piecemeal amendment of the Bankruptcy Code to change the result in a specific case. Not only is such retroactive legislation unfair, but it violates the principle of a neutral and fair bankruptcy procedure. This Subcommittee should not sanction such a use of the Bankruptcy Code to interrupt ongoing judicial proceedings.

S.46 would amend Chapter 11 of the Bankruptcy Code to require approval by state regulatory agencies before the bankruptcy court can confirm a utility's reorganization plan. Under current bankruptcy law, state and federal regulators must approve any rate changes proposed in a reorganization plan. However, those transactions that are necessary to reorganize and rehabilitate a troubled corporation -- such as restructuring the corporation, issuing new securities or debt instruments, and the like -- are within the exclusive expertise and control of the bankruptcy court. It should be noted that existing law does not exclude these non-bankruptcy regulators from the proceedings; they can comment on a proposed reorganization and contribute their partic-

ular expertise to the matter. However, these outside agencies may not control the proceedings; only the bankruptcy court has that role under the modern Code.

EEI believes that current law, which dates from the comprehensive revision of the bankruptcy laws in 1978, strikes the appropriate balance for reorganizations. After all, bankruptcy is an extreme state of affairs by definition, and the procedures for corporate reorganization are designed to suspend much of normal business so that the failing entity can be put back on solid footing in some way. A petition for reorganization under Chapter 11, as a result, stays various kinds of judicial actions, allows a bankrupt company to cancel certain contracts, and suspends the federal and state regulatory review of various transactions, necessary for revitalizing the company, that would otherwise be required outside the context of bankruptcy.

In addition to providing a bankrupt company this kind of "breathing space," modern reorganization procedures seek to make efficient use of this time to reconcile fairly and impartially all the competing interests in the reorganizing company and to expeditiously return it to the marketplace. Central to achieving an efficient and impartial process is the dominant role Congress gave to a neutral, judicial, politically independent bankruptcy court. By eliminating the multijurisdictional oversight of transactions under a reorganization plan that encumbered prior law, the 1978 Bankruptcy Code elevated the court to the stature of a neutral arbiter, with the requisite expertise, and well-suited to balancing the range of public and private interests involved in a bankruptcy.

S.46 seeks to abandon this sensible framework and restore approval of state public utilities commissions as a necessary condition for reorganizing a bankrupt electric utility. This requirement will result in delays from multiple determinations of

the merits of proposed reorganization plans and unpredictability from inconsistent or conflicting rulings of agencies claiming jurisdiction. Perhaps most importantly, this step backwards will not achieve anything of significance to equitable bankruptcy practice. Contrary to the claims of some, consumers are already protected by state control over retail power rates and by federal control over wholesale rates, a division of regulatory authority unaffected by the Bankruptcy Code.

Moreover, there is no sound basis for singling out electric utility bankruptcies for this change in Chapter 11 procedure. There is no unique attribute of such bankruptcies that warrants a return to pre-1978 law for utilities, but not for other corporations. The 1978 Code scaled back not only the role of state regulatory commissions, but also that of the Interstate Commerce Commission and of the Securities and Exchange Commission. These federal agencies have as significant -- and as discrete -- missions on behalf of the public interest as do state regulators, and could equally claim an exception from the Code's streamlining of reorganization proceedings. In truth, the uniform reduction of non-bankruptcy regulatory control over reorganization plans in 1978 means that S.46, if it is to be seriously advanced, would reopen that fundamental policy decision for reconsideration.

The 1978 revision of the bankruptcy laws followed months of careful, thoughtful deliberations based upon testimony from countless experts. The policy decision to streamline the reorganization process was not arrived at hastily. Now, in the face of the first electric utility bankruptcy under the new Code, proponents of S.46 want to reverse that policy before it has had a chance to work. We urge Congress not to act prematurely to change such a carefully considered course.

Of course, one other effect of S.46 is a change in the balance of federal and state authority in electric power regulation.

That balance is a function of federal law outside of the Bankruptcy Code. If Congress has a policy concern growing out of the present balance, it seems highly inappropriate to address it in the context of bankruptcy procedure. Certainly, EEI is not advocating that the balance needs adjustment, but if the question were to be examined, it should be in the context of the federal power statutes, and before the Committees with jurisdiction over them.

In sum, EEI believes that S.46 would single out electric utilities for special, inequitable treatment in Chapter 11 proceedings. This disparity would deprive them of the benefits of the sensible design for reorganization adopted by Congress so painstakingly in 1978. Moreover, the retroactive effective date for this bill adds a particularly harsh character to this discrimination, suggesting that it is permissible to change the rules during the game, since it is only electric utilities that are affected. We believe this bill lacks any merit, and we urge the Subcommittee to reject it.

Mr. Chairman, we appreciate the opportunity to submit this statement.

**Nuclear Information
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July 17, 1989

Dear Senator:

We, the undersigned, are writing to urge you to support the Electric Utility Bankruptcy Clarification Act (S. 46) which would ensure that electric utilities do not misuse bankruptcy filing to evade state laws and that state public utility commissions retain their full regulatory authority.

Until recently, no utility has declared bankruptcy since the Depression. However, the issue has become important because one utility has declared bankruptcy, and is attempting to use the bankruptcy process to circumvent state regulatory laws. Public Service of New Hampshire (PSNH) seeks to evade a state law which prohibits it from increasing its rates to recover its uneconomic investment in the Seabrook Nuclear Power Plant until the plant begins producing electricity.

As part of its bankruptcy filing, PSNH proposes to alter its corporate structure in a manner which would deprive the New Hampshire Public Utility Commission of its regulatory jurisdiction, in favor of the Federal Energy Regulatory Commission (FERC). PSNH then hopes FERC will step in, override state law, and allow PSNH to increase its rates by up to 40 percent. This is a much larger increase than is allowable under state law.

The passage of S. 46 would ensure that utilities could not misuse corporate restructuring to deprive ratepayers of those protections and that ratepayers would be protected by state laws regardless of a utility's financial status.

S. 46 should not be seen as a "New Hampshire Bill." While the most immediate effect of this bill would be on ratepayers in New Hampshire, it would benefit ratepayers in almost every state in the Union. Several utilities around the country are already experiencing financial difficulties because of imprudent and uneconomic investments. This bill would discourage them from using a bankruptcy filing to evade state regulations in order to secure higher rates, even if ratepayers are receiving no electricity from those investments.

We feel it is important that states be able to decide their own energy policies and to enact laws to protect their ratepaying citizens, with the assurance that those laws will be upheld and obeyed.

We urge your support for this important legislation.

Sincerely,

Michael Mariotte
Nuclear Information Resource Service

Daniel Borson
Nuclear Economics Analyst
Public Citizen

Bill Magavern
Staff Attorney
U.S. Public Interest Research Group

Environmental Action Foundation

1525 New Hampshire Avenue, N.W. Washington, DC 20036 (202) 745-4871

August 11, 1989

Sen. Howell Heflin, Chairman
Subcommittee on Courts and Administrative Practice
Committee on the Judiciary
U.S. Senate
Washington, DC 20510

Dear Chairman Heflin:

Environmental Action Foundation ("EAF") hereby submits its comments on S. 46, the Electric Utility Bankruptcy Clarification Act, for inclusion in the hearing record.

EAF is a nonprofit, research and educational organization concerned with energy and environmental issues. EAF has assisted or intervened on behalf of consumer organizations in numerous cases involving the restructuring of the electric utility industry.

The efforts of Public Service Company of New Hampshire ("PSNH") to use bankruptcy as an escape from state regulation come at time when the utility industry nationally is seeking to dilute its accountability to consumers, regulators and the free market. S. 46 takes an important step toward blocking those efforts.

Utilities Nationally are Seeking to Dilute Their Accountability to Consumers and Regulators

PSNH's proposal to use bankruptcy as a means to escape state regulation comes at a time when the electric utility industry at large is seeking to dilute utility accountability to consumers, regulators and market pressures. Traditional franchised utilities -- those with distribution or transmission monopolies -- no longer enjoy the certainty of rising demand, rising revenues and rising profits. Today's uncertainty is a product of several forces: (1) prudence disallowances; (2) customer conservation; (3) competition from existing market participants, such as municipal systems and rural cooperatives; and (4) competition from new generation entrepreneurs.

To escape these market and regulatory pressures, utilities are changing their corporate form. That restructuring activity -- creation of holding companies and utility affiliates -- generally enables utilities to reduce state oversight of future power plant construction, and frees utilities to compete unfairly against other entities in wholesale bulk power markets.

The controversy over Public Service of New Hampshire (PSNH) reveals yet another restructuring method: Bankruptcy. Other witnesses have explained how PSNH's restructuring would lead to evasion of state regulation. We agree with those comments and will not duplicate them here. Instead we will use this opportunity to emphasize two other points. First, utilities should not be free to use bankruptcy to escape the pressures of competition. Second, utilities should not be free to use bankruptcy to escape the consumer and investor protection requirements of the Public Utility Holding Company Act.

Utilities Should Not Use Bankruptcy to Escape the Pressures of Competition

The goal of public utility regulation is to subject utility managers to the discipline of the competitive market. That is what the New Hampshire legislature, and the New Hampshire Public Utilities Commission, have done in enacting and applying the anti-CWIP statute. To explain further:

In a competitive market, a seller is a "price taker," not a "price maker." That is, the individual seller does not set the price independently of market forces; market forces set the price and the individual seller accepts that price. If the seller attempted to raise its price above the market-set level, its customers would shift to other sellers. Thus the seller in a competitive market must accept the market reality that customers will not pay before a product before that product is available.

New Hampshire's anti-CWIP statute simply applies that reality to the regulated market. The statute says that PSNH cannot charge its customers for Seabrook electricity until its customers receive Seabrook electricity. Unlike its counterpart in the competitive market, PSNH does not or cannot accept that competitive reality. Therefore, it seeks to avoid through bankruptcy.

The proper way to beat the competition is to meet the competition: by strengthening management, finding new efficiencies, enhancing quality of service and lowering prices. Instead of meeting the competition, PSNH proposes to escape from it. S. 46 blocks that escape, for PSNH and for any other utility that cannot endure competitive pressures.

Utilities Should Not Use Bankruptcy to Escape the Consumer and Investor Protection Requirements of the Public Utility Holding Company Act

The logic of PSNH's preemption arguments extends well beyond the area of bankruptcy court-state commission preemption. PSNH has told the Bankruptcy Court that no "nonbankruptcy regulation" should apply where that regulation would be inconsistent with PSNH's reorganization plan. If PSNH is successful, its reorganization plan could preempt the Securities and Exchange Commission's enforcement of a critical consumer and investor protection statute: the Public Utility Holding Company Act of 1935, 15 U.S.C. sec. 79, *et seq.* ("the Act" or "PUHCA").

That result would be fatal to consumer protection. The Public Utility Holding Company Act is an essential statutory protector of competition and consumers in the electric industry. The Act's pre-acquisition review standards, under Sections 10(b) and 10(c), prevent restructuring which is anticompetitive, uneconomical or too complicated for regulators to untangle in subsequent rate proceedings. Moreover, the Act's ongoing financial monitoring provisions require the SEC to monitor the financial issuances and interaffiliate transactions of "registered companies." Finally, the Act limits utility investment in nonutility ventures. These provisions protect consumers and investors from the risks of, among other things, financial instability and cross subsidies.

More specifically, the Act (1) bars utility acquisitions which monopolize new territories or new power sources, or which create risks to consumers or investors, see Section 10(b)(1), (2), (3); (2) demands that utility acquisitions "serve the public interest by tending toward the economical and efficient development of an integrated public-utility system," see Section 10(c)(2); (3) limits utility speculation in unrelated ventures

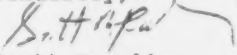
(e.g., banks, real estate, distant utility businesses), where that speculation imposes risks on electric customers, see Sections 1(b), 11(b)(1); (4) guards against corporate structures which make state regulation more difficult, see Section 1(b); (5) prohibits interaffiliate transactions within registered holding company systems, except at cost, see Sections 12 and 13; and (6) requires advance SEC review of certain bond issuances of registered holding company systems, see Sections 6 and 7.

If PSNH avoids application of PUHCA, it will be free to use its new holding company structure to compete unfairly in new markets, invest in risky nonutility businesses, and conduct other questionable transactions without review by the SEC.

We note that S. 46 as proposed does not explicitly protect against preemption of PUHCA by the bankruptcy court; it deals only with preemption of state commission regulation. While we would argue that the existing Bankruptcy Code does not authorize preemption of either state law or PUHCA, we would urge that the proposed legislation clarify this point.

We appreciate this opportunity to submit comments on S. 46. If you have any questions, please do not hesitate to call us.

Sincerely,


Scott Hempling
Attorney

Senator HEFLIN. We will be in recess for 3 minutes, and then we will have Mr. Stewart's confirmation hearing.

[Whereupon, at 12:05 p.m., the subcommittee adjourned, subject to the call of the Chair.]

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